Research Programme Consortium for Improving Institutions for Pro-Poor Growth

State-Business Relations and Economic Performance in Ghana

Charles Ackah,
Ernest Aryeetey,
Joseph Ayee
& Ezekiel Clottey*

Discussion Paper Series
Thirty Five
January 2010

IPPG Discussion Papers available at
www.ippg.org.uk

IPPG Programme Office, IDPM, School of Environment & Development
University of Manchester, Arthur Lewis Building, 2.023, Oxford Road
Manchester M13 9PL; Telephone 0161 306 6438; ippg@manchester.ac.uk
www.ippg.org.uk

*Charles Ackah and Ernest Aryeetey are researchers at the Institute of Statistical, Social and Economic Research, University of Ghana while Ezekiel Clottey is a PhD Candidate at the same institute. Joseph Ayee is a Professor in Political Science at the University of Ghana.
The authors gratefully acknowledge funding from the IPPG.
Charles Ackah is the corresponding author: cackah@ug.edu.gh.

Paper prepared for the DFID-funded Research Programme, Institutions and Pro- Poor Growth (IPPG). The authors are grateful to DFID for the funding that made this research possible. The views expressed in this paper are entirely those of the author and in no way represent either the official policy of DFID or the policy of any other part of the UK Government.

Material published by the IPPG may be reproduced free of charge in any format or medium provided it is reproduced faithfully, not used in a misleading context and properly attributed to the author(s). Copyright exists in all other original material published by members of the Programme and may belong to the author or to the University of Manchester depending on the circumstances of publication. Enquiries should be sent to the editor at the above address.

EXECUTIVE SUMMARY

The relationship between the state and business community in Ghana has varied since independence. Though each government has had distinct relations with business and private sectors, civilian governments have generally promoted and enjoyed good rapport with the business community while military governments especially in the 1980s have tended to have confrontations with the private sector. This study used a multi-disciplinary approach that included both qualitative and quantitative aspects of the disciplines of political science, economics, history, sociology and organizational management. To seek to understand what constitutes effective state-business relations, and to assess how state-business relations are related to economic performance, the study relied on historical institutionalist inductive theories- comparative historical analysis and path-dependence, among others. For this analysis, the study relied on both primary data, from interviews with selected formal and informal enterprises and regulatory agencies within Ghana, and secondary data derived from a review of statutory literature such as the Constitution of Ghana, Acts of Parliament, Statutes, Codes, Contracts, rules and procedures and conventions establishing institutions. The purpose here was to examine the characteristics of formal and informal rules and regulations governing the establishment and operation of foreign and indigenous businesses, how these have evolved over time and how they may have impacted economic performance.

For the quantitative economic analysis, the study used a panel of 256 Ghanaian manufacturing firms over the period 1991-2002 to analyze the extent to which an effective state-business relationship is beneficial to economic performance. Focusing on total factor productivity, we have found that an effective State Business Relations (SBR) or a sound investment climate correlates positively with better firm performance, possibly channelled via a more optimal allocation of resources in the economy. Concerning the effect of the investment climate indicators, our results show that an 'unfriendly' investment climate illustrated through firms' perceptions about economic and regulatory policy uncertainty affecting their operations and growth are negatively correlated with productivity. With regards to the SBR measures, we find that social networks as indicated through the extent to which firms or their managers have close contacts within the government or bureaucracy have a statistically positive correlation with firm performance. These results indicate that being well connected with those who make and implement government policy increases the chances of being able to lobby to overcome some of the difficulties confronting normal business enterprises, such as the number of procedures it takes to obtain licenses and permits and the number of days it takes to clear imported goods from the port.

Narrative analysis of state agencies and Private Enterprises Foundation's perceptions of SBRs in Ghana from 1992 to 2008 which also coincides and extends beyond the period of econometric analysis of SBRs on firm performance confirms the results discussed above. Both state and BAs agree on a shift from a predominantly ad hoc and informal clientelistic relationship to a more formal and synergistic SBRs in Ghana since 1992. Formal and regularized meetings between state agencies and businesses have positively impacted on firm productivity. For instance, PEF's formal advocacy role and function resulted in the use of GCNET to expedite clearing of imported goods. Business concerns of firms are channeled more often through formal by BAs to state agencies. Firms through their BAs make inputs into budget and other policy on formalized basis. Moreover, strong formal relationship between the executive and BAs such as the investors advisory council have helped firms stay close to government and bureaucracy.

Overall, our findings contribute to understanding the link between an effective state-business relations and economic performance. This paper adds to the work done by Qureshi and te Velde (2007) by investigating the key determinants of firm performance and also assessing the relationship between an effective SBR and firm productivity in Ghana. The results of the study stress the need for an enabling environment for the private sector. Experiences from East and Southeast Asian economies have also shown that investment and productivity growth critically hinges on an effective and vibrant private sector underpinned by a sound investment climate. Promoting a sound investment climate is one of the core responsibilities of the state in both developed and developing countries to achieve rapid capital accumulation and sustained growth and poverty reduction. Markets are good but are not without flaws. Thus, in order for inequalities in incomes and opportunities not to be exacerbated by the markets, it is important that the many constraints that inhibit the private sector from responding effectively to market incentives are removed, complemented with an increased effectiveness of government involvement in supporting private sector activities. Apart from the positive effect of SBRs on economic performance, the other lesson which can be drawn from the paper is that even though successive governments in Ghana have shown some commitment to supporting a viable private sector that commitment has, at the same time, been undermined by governments' own fear of a strong private sector acting as a countervailing force and thereby weakening their monopoly over neo-patrimonialism. Consequently, the commitment may be seen as a public relations hoax. An effective SBR in Ghana requires sustained formalized political commitment to policies that sees the private sector as a catalyst and initiator of pro-poor growth and development.

CONTENTS

1 INTRODUCTION

A number of theoretical models provide many compelling reasons why effective SBRs would stimulate economic growth and poverty reduction. Economic growth has been an important topic of discussion in almost every economy for a very long time. Previous research has found steady increases in investment and productivity to be crucial to a country's long-run economic growth and poverty reduction. Experiences from East and Southeast Asian economies have also shown that investment and productivity growth critically hinge on an effective and vibrant private sector underpinned by a sound investment climate. Promoting a sound investment climate is one of the core responsibilities of the state in both developed and developing countries to achieve rapid capital accumulation and sustained growth and poverty reduction.

The economic reform programmes introduced in many developing countries during the 1980's stressed the need for a propitious enabling environment for the private sector. Initially there were high expectations that a package of macroeconomic reforms ('getting the prices right') would give quick dividends in terms of economic growth. There has been growing disappointment with the growth record in many developing countries. Increased globalization and trade liberalization have led to a realization of the huge potential for the private sector but has also led to a considerable shift in the relationship between the public and private sector actors. Empirically, the size and role of the private sector is clearly evolving with globalization. Many high-growth nations have relied on markets to allocate resources. Markets, however, are not without flaws. And in order for inequalities in incomes and opportunities not to be exacerbated by the markets, it is important that the many constraints that inhibit the poor from responding effectively to market incentives are removed. A well-functioning market system, underpinned by strong institutions, with adequate protection of intellectual and physical property rights, and 'smart' interventions by the state, provides an enabling environment for businesses and individuals to innovate, compete and create value for all. This encapsulates the paramount importance of inclusive growth, i.e., creating economic opportunities through sustainable growth and making the opportunities available to all including the poor.

The relationship between the state and business in forging economic growth and development has been an enduring area of research for both economists and political scientists since the Industrial Revolution of the 17^{th} Century. Literature and research findings have emphasized both the positive and negative roles of the state in promoting markets and economic developments. By the early 1980s, many interventionist states had been judged to have failed in their quest to directly promote economic development. The public sector in most states became big and excessive, while government control of economic activities was counterproductive as pricing and subsidies favoured the urban few. Among developing countries, Import Substitution Industrialization (ISI) misallocated resources, discouraged exports and limited importation or transfer of much needed technology (Kohli, 2000).

Quite contrary to the neo-liberal economic views held by most international development agencies that state interventions in economic growth and development was counterproductive, the role of states in development and the enhancement of pro-poor growth cannot be overstated (Amsden, 1989; Wade, 1990). Notable examples of states like Japan, South Korea in the 1980s and most recently China and India in the late 1990s show the positive role states can play in promoting development and poverty reduction among developing economies. Chalmers (1982) shows that in the case of Japan the state's ability to prioritize areas for economic development, support private entrepreneurs and undertake direct and indirect interventions in economy promoted economic development. Such developmental states positively alter market incentive structures, manage conflicts, reduce risks and give direction to entrepreneurs (Kohli, 2000). Similarly, the World Bank Report of 1997 acknowledged the important roles of both the state and market, saying that "an effective state is vital for the provision of goods and services that allow markets to flourish and people to lead healthier, happier lives" (World Bank 1997:1). In short, the state also needs to establish and maintain the institutions that encourage or allow growth-related economic activity. While neoliberal growth theorists officially support a minimal role for government in economic affairs, it is still the case that economic growth generally depends upon a strong government and also relies on the state to construct and organize markets (MacEvan 1999:2-19).

Since independence in 1957, Ghana has been making slow and unsteady progress in achieving structural change and economic transformation. Successive Ghanaian governments have undertaken a number of reforms targeted at improving the investment climate and promoting private sector participation in the economy. In 1992, when the Fourth Republican Constitution was promulgated to usher in multi-party democracy, several other development policies were introduced to augment market interventions for sustainable private sector development. The country adopted and implemented neoliberal structural adjustment programmes and market reforms. Apart from pursuing a vigorous free-market economic, industrial and trade policy, it also adopted a liberalized investment policy, with the goal of attracting foreign investment as well as promoting joint ventures between foreign and local investors. Certain social, political and economic patterns of change have emerged, such as, an expanding private sector and the establishment of legal and regulatory structures. Some improvements have also been attained in the provision of infrastructure, health and education, macroeconomic stability, and ongoing reforms in the financial sector. These changes, however, are unlikely to guarantee the needs of the private sector in today's complex globalized world. Fundamental problems in the political and administrative system still persist despite many attempts at reform. Problems remain in relation to formalizing business operations in the country and corruption continues to be a problematic factor for doing business in Ghana. Many private companies encounter difficulties with regulations and continuing administrative inertia and corruption. A fairly high percentage of companies surveyed by the World Bank and IFC Enterprise Survey in 2007 report that they expect to pay informal payments to public officials to 'get things done' such as securing an operating license, meeting tax obligations and securing government contract. The survey also indicates that the burden of customs procedures in Ghana is quite cumbersome and constitutes a competitive disadvantage. Delays in customs procedures are sometimes deliberate as they create opportunities for officials to request unofficial payments.

Against this backdrop, the purpose of this study is to examine the efficacy or otherwise of institutional arrangements put in place by various governments since to promote state-business relations aimed at promoting economic growth and reducing poverty. The main objectives of the study are to:

- assess the political and economic factors that have either promoted or undermined the effective functioning of private sector growth in Ghana;
- identify and discuss the influence of formal and informal institutions on pro-poor policy decision- making and implementation; and
- examine the key determinants of state-business relations (SBRs) and their effects on corporate performance in Ghana.

The study takes a multi-disciplinary approach that includes both qualitative and quantitative aspects of the disciplines of political science, economics, and organizational management. Primary data include interviews with selected formal and informal enterprises and regulatory agencies within Ghana (we should indicate the people interviewed here). Secondary data include review of statutory literature such as the Constitution of Ghana, Acts of Parliament, Statutes, codes, contracts, rules and procedures and conventions establishing institutions. The purpose here is to examine the characteristics of formal and informal rules and regulations governing the establishment and operation of businesses, how these have evolved over time, and how they may have impacted on economic performance. For the quantitative economic analysis, the study uses micro-econometric methods based on firm-level data to investigate the linkages between measures of SBRs and firm performance. Cross-sectional and panel data regression analyses are employed to analyze how measures of effective SBRs relate to firm-level productivity.

2 CONCEPTUALIZING STATE-BUSINESS RELATIONS

Most development theories that emerged in the early 19th century discussed economic and political relations among both developed and developing countries. Many theorists commented on the relations between the state and society which also comprised economic groups. While development remained the overarching focus of such studies, much of what was discussed had direct bearings on the relationship between emergent states in the developing world and how economic agents interacted.[1] Then, the relationship between states and markets were conceived in ideological terms. Capitalists who wrote after Adam Smith emphasised the importance of markets in generating wealth. Most commentators claimed markets can self-regulate. Marxists writers on the other hand introduced class relations in how state and markets operate with claims that dominant classes who control wealth creation in most polities capture the state to pass laws and institutions that favour their cause. In between these two extreme positions on state and markets, many variant views were suggested to explain specific circumstances.

Conventional economic theorists see the state as "an important initiator and catalyst of growth and development" (Martinussen, 1997:220). What still remains contentious is how states are conceptualised. Martinussen (1997:222) lists two major approaches and four dimensions of the state. A 'society-centred' approach attaches much importance to societal structures and social forces that exert greater impact on what become the state such that state power, apparatus and functions derive from economic agents and social forces of societies (Poulantzas, 1978). 'State-centred' approaches give greater autonomy to state apparatuses and state personnel who act independently of economic agents, social classes or interest groups (Clark and Dear, 1984).

Myrdal's point about discretionary powers of political leaders is shared by dialectic modernization theorists like Jackson and Rosberg (1982) who noted that African rulers' personality takes precedence over rules. State-business relations take place in such political environments where patron-client relationships exist throughout Africa (Sandbrook, 1985). In the absence of a legal framework that ensures security of property; impartial public

[1] In Africa and for that matter Ghana, social scientists have been fascinated by the numerous analysis and conclusions they arrive at when they consider the role of nascent African states in fostering development. Many of such analysis have tended to directly or indirectly address the relationships between the states and businesses across the region.

services that directly facilitate production; and the regulation of foreign economic relations that maximises national interest, informal ties like blood relations, ethnic origins and personal access to political leadership dictate the pace of SBR in many parts of Africa.

More recently since the early 1980s, following the monumental role played by states in Asia to transform third world economies into developed states, many theorists have offered explanations on the role of states and markets (Johnson, 1987, Evans, 1995). Conclusions made by such scholars indirectly places emphasis on the 'magical' blend between the developmental goals of the state and the profit maximization drive of private sector institutions in Asia.

2.1 Macroeconomic Impacts

The factors responsible for market failure are the existence of monopoly, public goods (goods which are non-rival and non-excludable) and externalities. Others include imperfect and asymmetric information and increasing returns to scale. These factors disturb the optimal allocation of resources in the economy necessitating government intervention. For example, firms in their activities generate an externality which may end up affecting other firms or individuals with the cost or benefit of doing so not reflected in the value of their transactions. Similarly, these firms in the absence of training and adequate knowledge on the importance of investing in transferable worker skills, may under- invest in the skills and capacity of its general workers.

The government or public sector is also not exempt from failures. Government failure is said to occur when government action results in a less efficient allocation of resources. As such government intervention though necessary, may not be sufficient in addressing the failures in the market. This is because often, particularly in developing economies, governments lack the institutional and structural capabilities such as perfect information, practical and feasible development plans, essential logistics and structures that are required for addressing the failures which arise from the market. Also, government intervention in the market may result in crowding out which occurs when the government expands its borrowing more to finance increased expenditure or tax cuts in excess of revenue, crowding out private sector investment by way of higher interest rates. Similarly, government intervention activities may suffer intense lobbying and rent-seeking activities especially in countries with high records of corruption, eventually resulting in the misallocation of resources in the economy.

With this background, it is obvious that a SBR is extremely essential. Such a relationship provides the solution to state, market and coordination failures. In principle, business associations play a significant role in facilitating the formulation, implementation, and monitoring of economic policies and provision of feedback to the government (Hisahiro, 2005). In addition, such a relationship between the state and the private sector plays a central role in providing a bridge between the business community and political circles. Further, these relations establish communication links between the government and businesses to exchange wide-range economic information, such as on industrial development, export markets and research and development (R&D). In short, by establishing networks between the state and the market, concrete and practical data on industries, markets and technologies are obtained and shared which may serve as an important information bureau for effective industrial and state policies.

Harriss (2006) argues that a favorable collaboration between the state and business may have positive consequences for the growth of the economy as a whole, as long as certain mechanisms are in place which facilitate the following: transparency- the flow of accurate and reliable information, both ways, between the business and government; reciprocity between the business and the government; credibility- such that the market is able to believe what the state actors say and; high levels of trust through transparency, reciprocity and credibility. Hence, appropriate government policies, necessary for promoting economic growth in general and private sector development in particular are made possible by an efficient and fruitful state-business relations and dialogues.

2.2 Microeconomic Impacts

A well-structured, organized and effective relationship between the state and the market which satisfies the conditions of transparency, reciprocity, credibility and trust enhances the productivity of the firm in so many important ways.

Firstly, an effective SBR helps to reduce policy uncertainties in the economy. Expectations play a major role in the activities of firms and investors particularly when it comes to savings decisions, the type of investment to undertake or the type of goods to produce, the period of production, the quantities to be produced, the technology to be used, how and where to market what has been produced and even how pricing of the commodities should be done. All these decisions are taken based on anticipated market conditions and expected profitability. As such any uncertainty in the economy tends to affect the activities of these firms, the level of investment and consequently the level of economic activity, which translates into economic growth. The absence of clear policies causes these firms to operate in uncertain environments, exposing their businesses to undue risks and resource shortages. Dixit and Pindyck (1994) argue that uncertainty tends to have significant negative effects on investment, especially when investment involves large sunk and irreversible costs.

Against this backdrop, it is quite clear that businesses which have a better and effective relationship with the government may not be in the dark when it comes to policy decisions. Several studies confirm the negative effect that uncertainty has on investment. For instance, Bonds and Cummins (2004), in a survey of publicly-traded US companies, found that uncertainty has a negative effect on investment in both the short- and the long -run. Similarly, Ghosal (2003) was also able to show that periods of greater uncertainty have a crucial effect on industry dynamics and thus results in a decrease in the number of small firms and establishments and also a marginal increase in industrial concentration. In short, a greater correspondence and interaction between the state and the business enhances the free flow of information on prospective policies and reduce the level of uncertainty in the business environment, which is expected to result in a greater business confidence, quick firm-decision making and more accurate forecasting.

Secondly, an effective liaison between the state and the market results in tailor-made, accurate and efficient government policies and institutions. In other words, an effective SBR will ensure that government policies towards businesses are appropriate and of good quality. This is because, in the presence of such an effective relationship between the state and the market, the design of government policies will be done, among other things, using the input of and in consultation with the private sector. Regular interactions and sharing of information will ensure that the private sector objectives coincide with public action and that local level issues are inputted into the centralized policy processes. The private sector through that will be able to identify opportunities and constraints, as well as possible policy options for creating incentives, lowering investment risks and reducing the cost of doing business. This result in more efficient and convenient government regulations and policies such as tax regimes, licensing requirements and propriety rights obtained through policy dialogues and advocacy which will go a long way to reduce the risks and costs faced by firms and eventually enhance their productivity.

Finally, a good relationship between the state and businesses brings about an improvement in the quality, relevance and appropriateness of government taxing and spending plans. An effective relationship will help to ensure that certain facilities and mechanisms necessary for the survival of businesses are available and operational. This is because what motivates a firm to take risks, innovate and improve its performance depends crucially on the availability of certain services, much as it may depend on the private incentive facing the firm. Examples of these public services are good infrastructural system, information and communication technology, legal and judicial services, defense and security, availability of finance as well as the availability of human and physical capital. These facilities and systems affect the firms' productivity both directly and indirectly. For example, the provision of basic amenities like water and electricity affect productivity directly by facilitating the smooth running of businesses. On the other hand, the provision of infrastructure though may not directly affect productivity will indirectly enhance the transportation of inputs and output to and from the production sites which will enhance the speed of production and also the quality of marketed products and eventually enhance their productivity. The efficient delivery of these public services require an active participation of the private sector which will be responsible for lobbying the government to increase its spending in those areas, creating a more favorable environment for investment. Again, a good SBR is also able to stimulate and sustain innovation. Schumpeter (1940) explains that innovation is one of main forces behind firm dynamics and economic growth. Also, sometimes such collaboration between the government and businesses may result in the government taking the lead to encourage and motivate the private sector to engage in research and development by providing incentives, venture capital for new enterprises and also appropriate property rights. All these activities by the government affect the productivity of the firms directly and encourage further investment.

In effect, effective and sustained SBR can ameliorate both market and government failures, which are pervasive in most developing countries, and consequently bring about an increase in the growth of the economy.

3 CONTEXTUALIZING STATE-BUSINESS RELATIONS IN GHANA

This section borrows from earlier works done by Chingaipe and Leftwich (2007) in which they discussed factors that influence the relationship between the state and business. The institutional endowment of the state which comprises both formal and informal arrangements are key determinants of how states relate to businesses. The section attempts an analysis of institutional arrangements be it formal or informal by the various regimes in Ghana's political history and identifies the critical junctures that shapes the form of contemporary SBRs in the country. While some secondary data is used in the analysis, primary data gathered during the study is also analysed in looking at how business associations have been organized in the past and present.

SBRs in Ghana may be conceived from the point of view that the state as a result of colonialism was overdeveloped in relation to societal structure including economic agents (Alavi, 1972). For example, whereas the executive and judicial aspects of governance and some institutions like the military and civil service flourished during colonialism, legislative and democratic ethos remained neglected. Ake (1996) observes that colonialism as practised in Africa differed markedly from what took place in other continents as it was very statist in nature with complete control over land, labour, capital and infrastructure development. With absolute power, the British colonialists determined the structure of the Gold Coast (periphery) economy to supply raw materials for the industries in the United Kingdom (centre). Perhaps, it is through the colonial government's legislation on land that its relationship with the business community becomes clear. To begin with the Gold Coast Legislative and Executive councils had very few indigenes particularly chiefs as members. The passage of the Concessions Ordinance of 1900 enabled expatriate mining firms to enter the gold mining industry which was wholly African and eventually out-compete indigenous mining firms. In 1931, the colonial government passed a law making all lands in Northern Ghana public thereby forcing many to migrate to the south to work for both local and expatriate firms. The British did not only develop transport infrastructure that favoured cash crop farmers and mining firms but also established marketing and distribution boards that monopolised trade. Only wealthy expatriates and a few Africans benefited. The relationship between the colonial state and businesses resembled that of a master/servant as the state possessed more influence. Therefore, interest articulation and business associations possessed little influence on SBR at independence. Myrdal's (1968) 'soft state' concept gives ample insight into SBRs in Ghana as it depicts a considerable degree of discretionary power left in the hands of political leaders and state functionaries. Political leadership often drag their feet in imposing obligations on the governed as they themselves feel less obliged to abide by laid down rules. This leads to a situation where the government fails woefully to achieve its stated objectives, be it using the state as an economic agent in post independent Ghana.

The relationship between the state and business community in Ghana has varied since independence. Though each government has had distinct relations with business and private sectors, civilian governments have generally promoted and enjoyed good rapport with the business community while military governments especially in the 1980s have tended to have confrontations with the private sector. Civilian governments through constitutions (a) establish a rule of law that checks the arbitrary use of state coercive power by all citizens; (b) guarantees business representation in SBR organizations and institutional arrangements such as laws and acts of parliament; and (c) protects businesses and individuals rights of association and property among others. Military governments normally jettison the constitution and rule by decrees which do not necessary include the interest or views of the business community. The state in Ghana comprises of formal organizations like the executive, legislature, judiciary, ministries, departments and agencies (MDAs) and regulations such as the 1962 Companies Law, Ghana National investment Code, tax and patents regulations among others. The business community in Ghana includes formal and informal institutions and organizations that operate in the country's private sector. Formal private sector organizations include multinational firms registered in the country, locally-owned firms registered by the state, self-regulating bodies such as the Association of Ghana Industries (AGI), Empretec Business Forum of Ghana, and some non-profit organizations which have legal status. Most sole proprietor organizations which are not registered constitute the bulk of Ghana's large informal economy which employs over 80 percent of the workforce. The majority of informal organizations like farmer-based organizations, credit unions, retailers' associations, market women groups, transport unions, among others, are linked to the informal sector. In sum, firms, research and development organizations, educational organizations, the government, the regulatory agencies, information networks, financial organizations and the market all constitute the principal operating components of Ghana's SBRs.

Globalization and external economic pressures have also accelerated the transformation of state interventionist policies. Globalization has played an important role by forcing the state and business to revise their institutional arrangements. The government has over the years recognized the critical role of the private sector in the economic development. Several business associations including the AGI, the Ghana Employers' Association (GEA) and the Ghana National Chamber of Commerce and Industry and the Private Enterprise Foundation (PEF) have been presenting proposals on private sector development and ways to engage the private sector in formulating the annual budget and monitoring its implementation (to be discussed in details in section 4). The aim is to help increase government transparency on budget implementation and to develop private sector appreciation of problems in implementation and suggest possible solutions. The 2008 budget contains several initiatives aimed at improving the regulatory structures for doing business. There are talks about setting up a 'Better Regulation Task Force' to be charged with consolidating all the existing regulations.

3.1 Pre-Independence Era

Before independence, some appreciable level of relationship existed between the colonial government and business entities in the country even though the state often called the shots. The colonial government passed laws on land and commerce and offered protection for business concerns of particular interests such as commercial farming and mining. The Concessions Ordinance of 1900 that sought to settle rampant dispute in the land market and the piece of legislation passed in 1931 declaring all stool lands in the Northern Province public lands served as critical junctures in SBRs then as the mining industry became vibrant overnight with many expatriate firms prospecting. Likewise, making northern lands public sparked off massive out-migration of labour to feed the mines and commercial farms for cash crops such as cocoa in the south.

The business community responded to the boom in the mining industry by establishing a chamber of mines in 1928 for self-regulation and advocacy purposes. For cash crops, middlemen who bought cocoa formed associations to serve their interests and traded with less government interferences except for instances where litigation arose. The relationship between the colonial state and business community therefore appeared synergistic. Businesses were directed by the state into sectors preferred by the latter which also created incentives like good rail and road transport or secure cheap labour for the mines. The business community on its part organized themselves to patronise and promote the mining industry in the Gold Coast.

3.2 Nkrumah Regime

SBR during Nkrumah's regime served as a watershed for SBRs in post-independence Ghana. Formal and informal institutions and organizations established during the period as well as the structure of the economy have had tremendous impact on SBRs in the various regimes which with slight modifications have been path dependent.

Under the pretext that the private sector was practically non-existent save a few merchant companies like the United African Company (UAC), the regime revived the Industrial Development Corporation (IDC) which was established in 1948 to advance loans to Ghanaian entrepreneurs for industrial development. Nkrumah's government looked at the Indian, Israel and later other socialist country examples then and sent Ghanaians abroad to acquire skills for starting up businesses in Ghana (interview with K.B. Asante, December, 2008). The state shipping line, the Black Star Line (BSL), was fashioned on the Israeli example. Dan Morton Tailors is an example of the private enterprises that resulted from that initiative.

Perhaps, the most critical factor that determined SBR at the time was Nkrumah's socialist inclinations which were averse to private capital development. Through the Convention People's Party (CPP), Nkrumah supported and funded 'friendly' business associations (BAs) and enterprises that competed with other BAs and businesses often not associated with the CPP. Nkrumah believed that opposition businesses associated with his political opponents will use their economic power and influence to undermine his government. He therefore sponsored friends and CPP functionaries in business to complement the numerous State owned enterprises (SOEs) in the country. This resulted in a serious contest between the state and CPP favoured businesses and private enterprises and associations.

Therefore, SBR during the period was characterised by distrust, predation and a constant attempts by the state to weaken businesses not associated with it or the ruling political party. The period experienced many critical junctures such as the passage of pieces of legislation by the state to regulate land in Ghana; company laws and codes; and the establishment of several formal and informal organizations which shaped the SBR landscape. Within an economy of affection, these SBR developments naturally transcend into every sphere of Ghana's body politic and become a 'winner takes all' affair. Hence, opposition businessmen and political opponents of the Nkrumah regime sought assistance from the capitalist world to oust the CPP government in 1966.

The Nkrumah regime spanned both pre and post independent Ghana, commencing in 1951 when the CPP formed the first self government of the Gold Coast. Two dominant development policies took place during the period. From 1952 to 1959, what is known as the industrialization by invitation dominated SBRs while the statist development approach determined SBRs in the latter years of Nkrumah's rule. The CPP in the early 1950s was led by the lower stratum of petty-bourgeoisie who possessed small property and engaged in agriculture, commerce and various artisan professions (Ninsin, 1989:4). Having a feeling of economic inferiority to chiefs, the intelligentsia and older generation of merchants, the leadership of the CPP accommodated capital investment by foreigners. Encouraging local private entrepreneurs to invest in place of foreigners was tantamount to allowing political opponents to dominate the economy. Hence, British merchants managed the entire mining sector, 50 percent wholesale and retail trading as well as 74 percent of import trade was controlled by foreigners. Foreigners also controlled 90 percent and 77 percent of manufacturing and timber and saw-milling businesses respectively in the country (Ninsin, 1989:17).

Tangri (1999) notes that colonial policy to suppress Ghanaian entrepreneurs during colonialism resulted in the dominance of foreign and non-African capitalists in viable areas of the economy. This weakened the capacity of the private sector, particularly those outside the CPP to participate effectively in the economy. Thus, indigenous business groups had little influence over state power in decision making. By 1960 when Ghana became a republic, the country could arguably be labeled as a one party de facto state following nearly a decade of electoral victories won by the ruling CPP over other political parties. Then as one of the largest and most organized political parties in sub-Saharan Africa (Apter, 1965), the CPP under the tutelage of Dr Nkrumah was poised to carry out its socialist economic policies aptly conceptualised in the development plans that tasked the state and to a much lesser extent the private sector to lead Ghana's economic development. Dr. Nkrumah's socialist ideology therefore served as a major determinant of SBRs under his regime.

Nkrumah believed breaking out of poverty required a 'critical minimum' or 'big push'. In order to achieve the big push the state was to lead in the import substitution industrialization and planning as a substitute for market. The Industrial Development Corporation (IDC) which was set up in 1948 was charged to supervise a number of publicly owned commercial enterprises. These enterprises were originally intended to be transferred into private ownership once they became viable but Nkrumah abandoned the idea later when his socialist stance deepened in the 1960s. Nkrumah felt that "we (Ghana) would be hampering our advance to socialism if we were to encourage the growth of Ghanaian private capitalism in our midst" (Killick, 1978:37). This evidently runs counter to an earlier initiative taken in 1958 by Nkrumah to set up a committee to investigate the "best means of assisting Ghanaian businesses to overcome their difficulties" (ibid). It is instructive to note that the reasons for Nkrumah's suspicion and distrust of the private sector that included chiefs, intelligentsia and old merchants may be drawn from his socialist inclination.

As the first post-independence government, many pieces of legislation were passed to regulate business relations in the country. One instrumental law is the Industrial Relations Act of 1958 which was amended in 1960 and 1965 to streamline relations between employers (including the State) and employees, the majority of whom belonged to trade unions. Besides preventing labour related conflicts the act also spells out procedures for addressing grievances when they occur. The Companies Code of 1960 is another legal instrument passed by parliament to regulate both for profit and non-profit companies in the country. Business registrations, tax clearance, etc. are some of the key issues discussed in the company code. In 1963, the Capital Investment Act was legislated offering fiscal products and concessions to investors. The Land Registry Act 1962 (Act 122) also served as another decisive legal instrument which determined SBRs in the country as it gave the state full control over communal lands. Opponents of the government such as businessmen and chiefs were sidelined while CPP businessmen were rewarded with land for commercial farming.

Several organizations and business associations were established during Nkrumah's reign. These included organizations like the United Ghana Farmers Co-operatives Council (UGFCC), State Farms Corporation, Workers Brigade and the Young Farmers League. These organizations together with the Ghana Trade Union Congress were all organizations which had very strong links to the CPP government and were established to rival other business associations believed to be associated with the opposition parties. In the late 1950s, the CPP government through the Ghana Timber Marketing Board reallocated timber concessions in the country in favour of party supporters. In sum, SBRs under Nkrumah was one-sided as state power and influence was quite overwhelming.

3.3 NLC and Progress Party regimes

Following years of economic stagnation by the mid 1960s, opposition to Nkrumah's regime grew within and outside the state. The Cold War was peaking at the time and Western states were very disturbed about the socialist movement that was developing in Ghana and many parts of Africa. At the same time, Nkrumah's political opponents and some of his colleagues who had fallen out with him due to his strong socialist inclinations allied with the West to oust him. On the 24th of February, 1966, these developments succeeded in ousting Ghana's first president. The development strategy shifted from being statist to liberal where market forces and capitalism led by the private sector was preferred. In terms of SBRs, the new political leaders under the military junta, and later Dr. Busia's Progress Party (PP), dismantled the socialist machinery of the state and the CPP to create a new relationship between the state and private sector. The National Liberation Council (NLC) regime set up many boards to review SBRs in the country. Critical ones included boards that privatised SOEs and dealt with labour relations such as the Mills-Odoi Commission which reduced wages of workers in 1968. Many of such commissions were made up of moderate government officials who did not favour Nkrumah's socialist tendencies and private sector functionaries who did not benefit from the previous regime.

SBRs during the NLC rule are discernable in two main ways. First, the relationship lasted for a brief moment but registered a change in state dealings with the private sector in that the liberal market policies initiated by NLC implied some cooperation between the two sides. It must however be noted that the business side included two major factions namely businessmen who were favoured by the Nkrumah regime and businessmen who were aligned to the NLC/PP regime. In many instances, informal discussions between the NLC and businessmen involved the later group. Privatization of SOEs and the passage of special decrees to promote indigenous business reduced the predominance of the state over businesses. Secondly, labour organizations which represented businesses allied to Nkrumah and the CPP were either forcefully dismantled or made redundant.

In 1969 when Dr. Busia's civilian PP government took over from the NLC government, not much difference occurred in SBRs between the two governments as the latter continued with liberal market policies which favoured its main constituency of merchants, business owners and lawyers. Beginning with the 1969 Constitution, which established most SBR organizations such as the ministries of finance and trade, courts, office of the ombudsman etc., a major institutional arrangement in the management of land was introduced and therefore businesses reversed communal lands back to traditional landowners (Article 164:1). The Constitution effectively debarred the state from compulsorily acquiring land thereby safeguarding property rights in the country. In many respects, the constitution set the tone for SBRs during Busia's time in office. Hence one could say formality was mostly used in dealing with businesses. Most issues concerning businesses were discussed in parliament and enforced by designated formal institutions. For example, after several clashes with the Trades Union Congress (TUC) over wages and retrenchment of workers, parliament took a day to enact the Industrial Relations (Amendment) Act, 1971 (Act 383) which dissolved the TUC (Ninsin, 1989). Of course some informal relations existed as it was alleged that the Prime Minister tried in vain to plant an associate in office as secretary general of the TUC much earlier (Twum-Boafo, 1996).

Other major legal instruments passed by the PP government that shaped and defined SBRs included the Ghana Business Act of 1970 which gave monetary ceilings and restricted foreign nationals from engaging in economic ventures in certain sectors of the economy reserved solely for Ghanaians. The Aliens' Compliance Order of 1969 helped expel foreign and West African nationals, especially Nigerians without resident permits, from the country, which allowed about 200,000 Ghanaians to take up their jobs (Danso-Boafo, 1996:104). The Prime Minister was quoted to have defended these policies as what a government must do to remain popular.

In sum, SBRs under the Busia government were defined by the 1969 Constitution which was based on liberal market economic doctrines. The leadership sought to increase foreign investment in the country by appealing to developed states and multinational corporations as well as undertaking stringent monetary measures that indicated their preparedness to rely on the market and private sector for economic development. Though the government tried to promote and protect Ghanaian businesses, many workers and business owners (including farmers) complained about the hardship generated by the economic policies of the PP government. The government also devalued the Ghanaian currency, the Cedi, and imposed a development levy on public sector workers to promote rural development.

Worker agitations and direct protests against the government sparked off a series of public demonstrations which made the government unpopular. At the same time, the Industrial Relations Act had been passed in 1971 to abolish the TUC which was seen to be part of the defunct CPP. There were as many as 127 illegal workers' strikes involving 52,247 workers between 1970 and 1971 (Danso-Boafo, 1996:128). Some sections of the business community complained of being intimidated by the state. Meanwhile, some businesses which maintained very close association with the ruling government and its officials were said to be favorites of the state. The credibility and neutrality of some members of the PP government were questioned when it was revealed that some of them served on boards of private firms (Danso-Boafo, 1996:128).

3.4 NRC/SMC regimes

On January 13, 1972, riding on the back of the economic problems, workers' strikes and an innate desire to guard their 'corporate interests', the military led by Col. I.K. Acheampong overthrew Dr. Busia's civilian regime. The main economic policy was indigenization which involved among others an active promotion of entrepreneurial skills of many Ghanaians to engage in many forms of economic endeavours. Acheampong's government also naturalized some foreign owned firms like the Ashanti Goldfields Corporation and eroded the little confidence the Busia government instilled in foreign investors by refusing to settle external debts it perceived to be dubious.

Though the period had its fair share of labour strikes, SBRs initially improved as both the capitalist class and workers were encouraged by the state to own part of foreign businesses through business association (Ninsin, 1989:8). The regime also took some steps to promote business through the passage of the Investment Policy Decree, 1975 (NRCD 329) and the Ghanaian Enterprises Development Decree, 1975 (NRCD 330) (Ninsin, 1989:27). The National Board for Small Scale Industries (NBSSI) was established during the same period. The economic boom was short-lived as many of the fundamental problems such as the structure of the Ghanaian economy remained unaddressed. The ensuing decline of the economy corresponded with a stall in SBRs as corruption and rent–seeking thrived in astronomical fashions in the latter years of the Acheampong regime (Oquaye, 1979). Ninsin (1989) attributes this downturn to the consequence of the indigenization policy that only deepened the precarious relationship between the state, Ghanaian business owners and workers. Rising economic inequalities and an unprecedented increase in social vices across the country then precipitated the eventual revolutionary uprising that overthrew the regime.

The Armed Forces Revolutionary Council (AFRC) led by Flight-Lieutenant J.J. Rawlings and junior army officers, which replaced the Supreme Military Council (SMC) regime stayed in office for only three months and handed over power to a civilian government in September 1979. That short period of the AFRC recorded one of the worst treatments of business owners and even political leaders (including senior military officers) in the country as they were perceived as exploiters who profited at the expense of a poor majority. Human and property rights were discarded indiscriminately by both the AFRC and the masses as wanton destruction of life and property of businesses and politicians brought economic mayhem and political instability into the country (Oquaye, 1979).

3.5 Limann's PNP regime

Dr. Hilla Limann's People's National Party (PNP) civilian government took over power from the AFRC in September 1979. Except for 66 and 51 workers strikes in 1980 and 1981 respectively, little took place in the area of SBR as the government stayed in office for only 27 months. Many state institutions and business people were yet to recover from the shock of the political upheavals that took place in 1979. Besides, the global economic crisis compounded and reduced the options of the Limann administration. It was still debating on how to deal with these problems when the Provisional National Defence Council (PNDC) led by J.J. Rawlings staged another coup in December 1981.

3.6 PNDC and NDC regime

SBRs in Ghana since 1993, when the Fourth Republican Constitution was promulgated, seem to mirror what formal and informal relations existed between the state and business right from the colonial era through the various state formation processes of post independent Ghana. Depending on the ideology and political orientation of the government in power, SBRs have taken many forms, ranging from acrimony, distrust, suspicion and tension to modest collaboration and consensus building. Governments with socialist ideology have tended to be more reliant on the state to achieve economic development while others which project liberal democratic ideals have relied more on market forces in allocating goods and services. Beside popularly elected governments, Ghana's political economy has been shaped to a large extent by military juntas which had longer spells of political power in the first three republics. Under these military dictatorships, SBRs generally tended to be characterised by distrust, suspicion and fear of violent reprisals from the military leaders and their cohorts. Generally, the high incidence of political instability experienced by the country in the first 35 years after independence adversely affected SBRs in Ghana.

The structure and practice of SBRs in Ghana is also determined by state economic institutions and organizations (1992 Constitution, laws, ministries, departments and agencies) which are generally managed by bureaucrats and politicians. Such state institutions formulated and implemented economic policies that regulated the activities of the private sector. The private sector in Ghana is determined by ownership, control and management of organizations and institutions. Therefore, all institutions and organizations that fall outside the ambit of state or governmental ownership, control and management may be considered to be part of Ghana's private sector (LECIA, 2000:99). Ghana's private sector includes the large informal sector engaged in agriculture, commerce and traditional small scale processing and manufacturing as well as all privately owned local and foreign business concerns that operate in the more regulated formal sector of the economy. The private sector in Ghana also includes Business Associations (BAs), cooperatives, credit unions, financial institutions, savings and loans companies etc. The key needs of the private sector include available financial resources and reduced cost of capital; skills and entrepreneurial competence; ready and available market outlets within and outside the country that provide prospects for growth through innovation; and trade facilities which enhance payments, business linkages, networking and information sharing, among others.

Under the Rawlings leadership, SBRs developed in many ways ranging from continuity to massive policy changes that set the basis for a redefinition of SBRs in Ghana's Fourth Republic. In order to do a good analysis the period may be divided into two periods. The first period (1982-1992) entails discussions of the development of SBR before the country returned to democratic constitutional rule in 1992 while the second period (1992-2000) deals with SBRs in the post-constitutional phase. Starting as a radical populist government fiercely opposed to capitalism, the economic decline and outbreak of drought, energy crisis, and an overgrown and inefficient state prompted a quick turnover by Rawlings' Provisional National Defence Council (PNDC) regime towards negotiations with international development agencies like the IMF and World Bank. Persuaded that market forces would have greater discipline for individual economic behaviour than the state, Rawlings had no choice than to agree to the economic recovery programme (ERP) in April 1983 (Ayee et al, 1999:25). The main objectives of the ERP sought to realign relative prices so as to encourage more productive economic activity; reverse government policy of greater reliance on central planning and state controls of the economy towards dependence on market forces in production; and to improve government fiscal and monetary performance.[2] In fact, Ghana was the toast of many development agencies for implementing what came to be called Structural Adjustment Policies (SAP) introduced by the Bretton Woods institutions throughout the developing world. Between the mid-1980s to the early 1990s, the Rawlings regime implemented many other SAP policies that affected SBRs.

It must be noted that many private businesses as well as SOEs were not performing well. Business associations were therefore not very functional, members were not paying dues, and meetings were not regular. As a military government little resistance stood in its way in making decrees. Consultation between the regime and business community came up much later towards the end of the decade under the auspices of the World Bank and IMF (Ayee et al, 1999). These include the retrenchment of public sector workers, commencement of a policy of decentralising public administration in the country and reforming the civil service. Another policy that indicates a real shift from direct state participation in the economy was the proposed privatization of the SOEs through the Divestiture Implementation Committee (DIC) in 1988.

Decentralization and civil service reform were two policies that also aimed at improving the performance of state institutions in direct participation in the economy as well as facilitating business activities in the country. Many businesses at the time complained of the high cost of doing business in the country citing corruption, over centralization of authority and ineffective regulatory institutions. Though business participation remained minimal at best, some informal consultations between state authorities and leading businessmen generally helped to improve processes and outcomes. With regards to privatization of SOEs in Ghana, though the government initially failed to include the TUC and representatives from the business sector, public protest for business and civil society compelled state authorities to include the TUC and private sector (Ayee et al, 1999:26). By 1996, nearly 180 SOEs representing 60 percent of the lot had been divested.

SBR during the PNDC era owes much to the influence of external agents like the donor institutions which tried to eliminate the mistrust between the state and businesses in the country (Ayee et al, 1999:29). Until 1988 when both sides met publicly, the public sector dominated the reform process without much feedback from the private sector on economic reforms. Business perception of the PNDC government was tainted with mistrust and fear as leading businessmen had been dragged before the National Public Tribunal (outside the judicial system) and charged with crimes of economic sabotage (Tangri, 1999:84). Even major BAs like the AGI and GNCC lacked the wherewithal to engage or make meaningful contributions towards economic reforms. Some entrepreneurs were detained over long periods without charges. Many businesses suffered adversely from economic policies of the PNDC. Statements by PNDC officials were confrontational as some often hammered on improprieties and ostentatious lifestyles of businessmen (Tangri, 1999:87).

Nonetheless, an informal private sector think-tank was formed at the Ghana Investment Centre (GIC) which later transformed into the Private Sector Consultative Committee. After several meetings held in an atmosphere of mistrust and rancour the group collapsed late in

[2] Many scholars have commented on the outcomes of the ERP (see Ninsin, 1989; Aryeetey, 2000; and Ayee et al, 1999).

1989 (Ayee et al, 1999:30). Prior to and after an investor conference held in Ghana in February 1990, government continued to hold informal talks with the private sector until 1991 when a formal SBR consultative mechanism, the Private Sector Advisory Group (PSAG), materialized. It is believed that pressure from the World Bank was instrumental in its establishment. With the Minister of Finance as the main representative of government, the PSAG was tasked and supported by technical staff at the Ministry of Finance to "examine all existing laws and regulatory procedures which impeded private sector investment and development; advise the government on relevant revisions of obstructive laws; and to develop a set of specific recommendations for legal reform and simplification" (Ayee et al, 1999:31). Though the PSAG lasted for a brief period and collapsed before the 1992 multi-party elections, it was deemed to be successful in that its main recommendations were implemented by the government.

In January 1993, the PNDC military government transformed into a democratically elected government under a new name - National Democratic Congress (NDC) - with Rawlings and many of his PNDC comrades as leaders. SBRs continued with the establishment of the Public Sector Roundtable (PSR) in June 1993. Though it represented a larger section of the private sector and had Mr. P.V. Obeng, the Presidential Advisor on Governmental Affairs (PAGA), as its chairperson, it failed for many reasons to impact on decision-making as many differing opinions emerged among the PSR, which also had no clear mandate compared to PSAG (Ayee et al, 1999). The Private Enterprise Foundation (PEF) was formed in 1995 with representation from the majority of the large BAs like the AGI, GNCCI, GUTA, Ghana Chamber of Mines and the Federation of Associations of Ghana Exporters. As an institution tasked to perform advocacy for Ghana's private sector, PEF has had good collaborations with state institutions and has been quite assertive in its role to promote the private sector.

3.7 The NPP regime

In January 2001, the opposition New Patriotic Party (NPP) led by J.A. Kufuor took office after defeating the incumbent NDC in the 2000 presidential and parliamentary elections. As a party drawn from the moderate conservative market-friendly tradition of the United Gold Coast Convention (UGCC), it was little surprise that the NPP was committed to continue the market-friendly policies and initiatives began by the NDC and even pledged to advance a 'Golden Age of Business' in Ghana. The NPP envisaged that the pursuance of a liberalised trade, investment and industrial policy will attract local and foreign manufacturers, entrepreneurs and traders to establish value-added job opportunities for a significant growth in labour-intensive export industries in Ghana (Arthur, 2006:37).

Economic policies of the NPP government were generally geared towards supporting the growth of the private sector. One clear example was the establishment of a Ministry for Private Sector Development (PSD) soon after assuming office. This ministry which was later merged with the Ministry of Trade and Industry embarked on comprehensive public-private partnerships (PPP) known as the President's Special Initiative (PSI) that sought to identify and develop potential business opportunities in Ghana. PSI investments targeted salt, cassava, starch, textiles and garment industries in which Ghana was considered to have both comparative and competitive advantage over her neighbours in the sub-region (Apraku, 2002). The rationale for the PSI served several ends. In the case of cassava and the starch industry, government was offering many farmers opportunity to expand their yield as well as eventually owning the starch factory pre-financed by the government. The state's involvement in the textile and garment industry was to put the industry in a position to export garments and textiles for much needed revenue to the state and private businesses involved in the African Growth and Opportunity Act (AGOA) trade facility extended by the US government to African countries. The NPP government enhanced the Free Zones Board concept initiated by its predecessor (NDC) and also established the Export Development Fund (EDIF) soon after taking office in 2001.

To make its 'Golden Age of Business' pledge come true, President Kufuor held biannual meetings with the Ghana Investment Advisory Council (GIAC) that represents the leadership of BAs to obtain feedback on the economy and forge common goals for economic development in Ghana (Arthur, 2006:40). In addition, before the government presents the budget to parliament, the private sector meets to deliberate on the budget and make recommendations. The active participation of the private sector in Ghana's budgetary process throughout the NPP term in office gives credence to some positive development in SBR in the country. Under the NPP, state organizations like the bank of Ghana and MoTI & PSI commissioned several studies and research on Ghana's private sector. These studies resulted in the establishment of the MASLOC scheme, Venture Capital Fund, Business Assistance Fund (BAF) and several bilateral loans and credit facilities advanced by government to the private sector through participating financial institutions.

Despite the foregoing, several challenges were present. Awareness of corporate governance in general and of corporate social responsibility in particular, was low. The Companies Code, which provides the main corporate governance framework for registered companies, is robust yet out of touch with current developments in corporate governance and is in need of updating. Formal state organizations such as the Ministry of Trade and Industry, NBSSI, the Ghana Investment Promotion Centre, and some business associations like the AGI, PEF, General Agriculture Workers Union (GAWE), Ghana Employers Association (GEA), and EMPRETEC Ghana that are active in promoting good corporate governance, are weak in terms of finance and human capital.

In sum, over the past two decades, two major events have served as critical junctures for state business relations in Ghana. The first was the global shift towards a uni-polar world with neo-liberalism as the reigning ideology. Globalization and the liberalization of the economy in recent years have led to a palpable growth in the private sector in Ghana. As far back as 1989 the state under the auspices of the IMF and the World Bank initiated a new relationship with the private sector that has progressed from informal to a more formal and institutionalized relationship. The second critical juncture that has helped accelerate the pace of improving SBRs in Ghana has been the return to constitutional rule in 1992.

4 POLITICAL AND ECONOMIC ANALYSES OF SBRS ON FIRM PERFORMANCE

The extent and role of effective SBR as important determinants of firm level performance in developing economies, is burgeoning both on the theoretical side as well as on the empirical side (see Harris, 2006; te Velde, 2006; Qureshi and te Velde, 2007; Sen and te Velde, 2009; among many authors). This section specifically seeks to assess the extent to which SBR impact firm-level performance in Ghana. Using the World Bank Regional Project on Enterprise Development (RPED) survey data on manufacturing business establishments in Ghana, we now analyze the extent to which effective SBRs impact the performance of firms operating in Ghana. Specifically, our analytical approach is to examine how relations between the state and businesses in Ghanaian relate to the performance of business establishments in the country. We use regression techniques to relate firm performance measures to investment climate and SBR indicators. Our modeling approach is similar to the work by Qureshi and te Velde (2007) for Zambia but differs markedly in a number of respects. In particular, in addition to the LP approach adopted in their paper, which is followed also in the present study, we also employ the Systems GMM estimator to analyze a dynamic version of the standard production function. The RPED firm level panel dataset is the main data for the econometric analysis, meaning we are also able to deal with the problems of unobserved firm-specific heterogeneity and simultaneity biases.

4.1 Empirical Approach

4.1.1 Measuring Firm-level Productivity

Productivity determinants are complex and cannot be adequately described through simple tabulations. In order to allow for multiple factors to characterize firm performance simultaneously, this paper turns to regression analysis. Our baseline specification is a standard Cobb-Douglas production function which links output with inputs and the firm's productivity, as follows:

$$Y_{it} = A_{it} K_{it}^{\beta_k} L_{it}^{\beta_l} e_{it} \qquad (1)$$

where Y_{it} is real output (or value added), A_{it}, K_{it} and L_{it} denote total factor productivity (TFP), capital and labour of firm i in period t, respectively, and e is a random disturbance term. Taking natural logarithms and re-arranging slightly, we obtain

$$y_{it} = \beta_0 + \beta_l l_{it} + \beta_k k_{it} + w_{it} + \varepsilon_{it} \qquad (2)$$

where lower case letters denote log values, $w_{it} = \ln(A_{it})$ and $\varepsilon_{it} = \ln(e_{it})$. Firm productivity is an unobservable firm characteristic, which can be recovered from estimating the production function (2) using actual input quantities. The basic problem in estimating (2) is that the input variables are in general correlated with the unobserved productivity shock, w_{it} but might not be observed by the econometrician, leading to the well-known simultaneity problem in production function estimation.[3]

Several solutions have been proposed to address this econometric problem. In the most recent best-practices, firm-level TFP is calculated following the innovations espoused by Olley and Pakes (1996) that corrects the simultaneity bias arising from the fact that firms choose their levels of input once they know their levels of productivity.[4] The method also corrects the selection bias induced by the fact that firms choose to stay or exit the market depending on their levels of productivity, which in turn depend on the levels of their fixed factor input, namely capital stock. The authors propose to overcome the simultaneity problem by using the firm's investment as a proxy for unobserved productivity shocks.

Other best-practice methods such as the within-group and GMM-type estimators (e.g., Arellano and Bond, 1991) have also been extensively employed to correct for simultaneity biases but it is believed that (if properly done) the Olley-Pakes estimator has several advantages as it does not assume that the firm-specific productivity component w_{it} "reduces to a 'fixed' (over time) firm effect………..and hence is a less costly solution to the

---

[3] There are problems with estimating equation (2) with OLS; the method could be biased and would yield biased estimates of *TFP* if it turns out that the productivity shock in (2) is not orthogonal to the factor inputs as is implicit in OLS. See Marschak and Andrews (1944); Olley and Pakes (1996); Griliches and Mairesse (1998); and Levinsohn and Petrin (2003).

[4] For example, if more productive firms are more likely to hire more workers and invest in more capital due to higher current and anticipated future profitability, estimation methods such as OLS will not be consistent and thereby result in biased coefficient estimates; the estimated input coefficients would be higher than their true values.

omitted variable and/or simultaneity problem" (Frazer, 2005:592).[5] The problem with the Olley-Pakes estimator is that the procedure requires strictly positive investment, meaning that all observations with zero investment have to be dropped from the data. This condition may imply a considerable drop in the number of observations because often firms do not have positive investment in every year.[6] More recently, Levinsohn and Petrin (2003) propose an estimation methodology that corrects the simultaneity bias using intermediate input expenditures, such as material inputs, as a proxy. This is especially useful as there are many firm-level datasets containing significantly less zero-observations in intermediate inputs than in firm-level investment. Since the Levinsohn-Petrin technique imposes less stringent data requirements than the Olley-Pakes approach, we follow several recent studies by choosing to adopt the former for the estimations in this paper.[7]

4.1.2 Estimation Strategy

We follow a two-step estimation procedure. In the first step, we estimate equation a production function to obtain a measure of the total factor productivity of firms. We use the Levinsohn-Petrin method to estimate equation (2) to correct for the presence of selection and simultaneity biases in the input coefficients required to construct the measure of TFP.[8] The dependent variable we use is gross revenue (rather than value added) and that the GMM estimator is used. In the second stage, we relate firm productivity to SBRs exploiting the variation in productivity over time and across firms. Specifically, we estimate an equation where TFP is explained by a set of firm characteristics and investment climate indicators. Unlike Qureshi and te Velde (2007), we control for lagged productivity since we believe that TFP determinants are highly persistent. Moreover, in contrast to Qureshi and te Velde (2007), who runs OLS estimations of this equation, we prefer to use a generalised method of moments (GMM) framework. Indeed, we control for other crucial and observable firm characteristics such as, average education and average age of employees, age of firm, foreign capital, export status, location and firm size that may influence firms' reaction to the investment climate. However, these characteristics are not strictly exogenous and OLS estimations may lead to biased and inconsistent estimates.

To explain TFP at the firm level, we use the following framework:

$$TFP_{it} = \alpha_0 + \alpha_1 TFP_{it-1} + \beta' X_{it} + \phi' SBR_{it} + \eta_i + \eta_t + \varepsilon_{it} \quad (3)$$

where TFP_{it} is total factor productivity at the firm level, X_{it} is a vector of firm characteristics, SBR_{it} is a vector of a number of investment climate indicators, η_i represents the unobserved firm-specific factors, η_t is time-specific effect which takes into account macroeconomic shocks common to all firms, ε_{it} is the time-varying error term, and

[5] Others have raised doubts about the appropriateness of the estimator's internal' instruments (past levels for current differences and past differences for current levels) as they are likely to possess little resolving power (see Griliches and Mairesse, 1998).
[6] For example, in the specific case of the data set under examination, about 32 percent of observations has zero investment while a further 44 percent has "missing" investment and therefore much information would be lost in dropping these observations, as required by the Olley-Pakes technique.
[7] See Levinsohn and Petrin (2003) for further details on the methodology. We implement this procedure using the 'levpet' command in STATA, which was written by Levinsohn, Petrin and Brian Poi (2004).
[8] The coefficients of the variable and fixed factor inputs are estimated at this stage. Notice that we include real value of firm's intermediate inputs as additional variable factor input before estimating equation (2).

α, β and ϕ are parameters to be estimated. The subscripts i and t represent firm and time period, respectively.

Clearly, equation (3) is a dynamic model with a lagged dependent variable. Several approaches have been used to estimate (3) in the empirical literature. As many economists have pointed out, the estimation of equation (3) presents at least two main important econometric difficulties that may lead to inconsistent and biased estimates: omitted variable bias and endogeneity bias. The term η_i is a permanent but unobservable firm-specific effect and captures the existence of other productivity determinants that are not already controlled for by the vectors X and SBR (i.e. omitted variables). It is time invariant and generally captures such cross-sectional heterogeneity as differences in preferences or tastes or technology between firms. If the firm-specific parameter were not included in (3), random firm-specific fluctuations would be grouped into the regression residual ε_{it}. This would bias the common error term. In the presence of any correlation between the right-hand side variables and the firm-specific effect (η_i), estimation methods such as OLS will not be consistent.[9]

Aside from omitted variable bias, cross-sectional regressions may suffer from endogeneity problems. Note that the determinants right-hand side variables can be classified according to whether they are strictly exogenous, predetermined or endogenous.[10] The vector X is strictly exogenous if it is uncorrelated with all past, present and future realisations of ε_{it}. However, this assumption is rather too restrictive and often times very difficult to justify. For example, an unanticipated shock to the output of a firm could have a contemporaneous effect on the foreign capital share in the firm or the firm's decision to export, thus compromising the strict exogeneity of these variables. Alternatively, it is reasonable to infer that a positive shock to output in period $t-1$ will result in a higher level of foreign capital share or positively affect exports in period t.

The possibility of endogeneity together with the presence of firm-specific effects correlated with some of the explanatory variables implies that estimation methods such as OLS will not be consistent. A first step in obtaining consistent estimates is to eliminate the firm-specific heterogeneity. One approach is to employ the within-group estimator by taking deviations with respect to individual firm means. However, when the model includes a lagged dependent variable the dynamic fixed-effects model produces estimates that are inconsistent if *N* (number of firms, or cross section) is large relative to *T* (number of time periods), hence the fixed effects estimator is biased (see Nickell (1981) and Wooldridge (2002)). Specifically, the within-group estimator is biased downwards of the order $1/T$ and this bias declines as T increases. As we will discuss later, in this study, the number of time periods is small ($T=5$) and thus the bias could be severe. The GMM estimator proposed by Arellano and Bond (1991) relies on first-differencing to eliminate unobserved individual-

[9] In a pure cross-sectional regression, the unobserved firm-specific effect is part of the error term. However, in a dynamic regression the lagged dependent variable will by definition correlate with η_i and thereby result in biased coefficient estimates.

[10] For a variable z_{it} that belongs to the vector $\mathbf{X}$, z_{it} is said to be endogenous if it is correlated with ε_{it} and earlier shocks but uncorrelated with ε_{it+1} and subsequent shocks. By predeterminacy, we mean that $\mathbf{X}$ and ε_{it} are uncorrelated, but $\mathbf{X}$ may still be correlated with ε_{it-1} and earlier shocks.

specific effects (η_i), and then uses lagged values of endogenous or predetermined variables as instruments for subsequent first-differences.

First-differencing equation (3) yields

$$y_{it} - y_{it-1} = \alpha\left(y_{it-1} - y_{it-2}\right) + \beta'\left(X_{it} - X_{it-1}\right) + \phi'\left(SBR_{it} - SBR_{it-1}\right) + \left(\varepsilon_{it} - \varepsilon_{it-1}\right) \quad (4)$$

However, eliminating the country-specific effect introduces a correlation between the lagged dependent variable and the new error term. Due to the correlation between y_{it-1} and ε_{it-1}, it can be shown that

$$E\left(y_{it-1} - y_{it-2}\right)\left(\varepsilon_{it} - \varepsilon_{it-1}\right) \neq 0\,. \quad (5)$$

To address the endogeneity problem, Arellano and Bond (1991) recommend using the lagged values of the explanatory variables in levels as instruments under the assumptions that there is no serial correlation in the error term ε_{it} and the right-hand side variables. Thus, the GMM estimation procedure simultaneously addresses the problems of correlation and endogeneity. The consistency of the GMM estimator depends on the validity of the assumption that the error term does not exhibit serial correlation and on the validity of the instruments. By construction, the test for the null hypothesis of no first-order serial correlation should be rejected under the identifying assumption that the error is not serially correlated; but the test for the null hypothesis of no second-order serial correlation, should not be rejected. We use two diagnostics tests proposed by Arellano and Bond (1991) and Blundell and Bond (1998), the Sargan test of over-identifying restrictions, and whether the differenced residuals are second-order serially correlated. Failure to reject the null hypotheses of both tests gives support to our model.

4.2 Measuring SBRs in Ghana

The role of institutions in development has received increasing attention in recent years. The institutional environment forms the framework within which individuals, firms, and governments interact to generate income and wealth in the economy. The institutional framework has a strong bearing on competitiveness and growth. Many economists hold the view that bad institutional environments keep returns to capital low and therefore hold back economic growth. Could it be that Ghana's growth is being compromised by the quality of the institutional environment? The World Economic Forum Global Competitiveness Index ranked Ghana 102nd out of all 134 countries covered in the world in 2008 in terms of the overall competitiveness of the country (World Economic Forum, 2009).

Effective SBRs is fundamental in promoting formal businesses, investment, and economic growth. In practice, however, finding credible measures of SBRs that describe adequately the various facets of state-business interactions and yet do not suffer from the well-known problem of endogeneity has been difficult as the literature on measurement of SBRs is still developing. Some even maintain that attempting to measure a relationship is a hopeless exercise (Te Velde, 2009). Yet, a review of the empirical literature would throw up a large number of indicators that have been employed as proxies of effective SBRs, including both subjective indicators about perceptions of government effectiveness and objective indicators about the investment climate as in the World Bank's *Doing Business Reports* (e.g., number of procedures to obtain a license).

In line with the recent empirical literature, in this study, we use several elements of the institutional and policy environment (i.e., the investment climate) in Ghana as proxies for effective SBRs[11]. We analyze the factors - both those related to the overall business environment (e.g., institutions, infrastructure, policies, etc.) as well as those internal to the individual firms (managerial ability, input costs) that affect firm level productivity and, by extension, the productivity of the overall economy. Due to data constraints, we are only able to consider the following elements of SBRs:

i) the firm's perception about economic and regulatory policy uncertainty affecting its operation and growth; and
ii) social network – the number of politicians and civil servants 'known' by the firm.

We now discuss each of these two elements in turn:

i) Firm's perception about economic, regulatory and institutional environment

The literature shows clearly that the scope and quality of the regulatory and institutional environment in which firms operate affect their investment decisions and productivity. The government has a responsibility to regulate the activities of private entrepreneurs in order to avoid market failures that may disadvantage firms and consumers. However, overregulation may impose substantial costs on businesses and deter productive investment or result in misallocation of resources (Kerr, 2000). Theoretical research has suggested that effective SBRs result in a reduction in uncertainty concerning the investment environment, which positively affects the firm's performance. As such, to measure how effective SBRs are, there is the need to include the firm's objective opinion about how changes in government policies and regulations impact the firm's operations and growth. The lower would be the effectiveness of SBRs the greater the problem of uncertainty.

ii) Social network- the number of politicians and civil servants 'known' by the firm

The role of social networks in Africa is crucial and paramount, whether in private life or in the area of business. In the presence of market and state failures, social networks play a very critical role in the ability of businesses to overcome red tapes and other constraints. One important measure is to use the extent to which firms or their managers have close contacts within the government or bureaucracy. The RPED data includes questions on social network, providing information on each firm's social connectedness within the government or bureaucracy. We use this information to test whether productivity rates are higher among those firms who are better socially connected and have 'friends' in government.[12] Since political networks appear to be particularly important for firms we focus on the way such networks affect the productivity of firms. We study if firms that are well 'connected' with the government bureaucrats are able to overcome the well-known market and

[11] See Hyden et al (2004); Kaufman et al (2005); and Qureshi and Te Velde (2007) for examples.

[12] Maintaining political networks or being well connected within the civil service may be legitimate behavior, but in an environment where rules of conduct and institutions are weak, this may exacerbate political and economic corruption. In Ghana, as in many developing countries, institutions are either non-existent, poorly developed or poorly enforced. As a result, rules of conduct may be ambiguous, resulting in bribery, extortions, nepotism, biased bidding procedures and other undesirable behaviours.

government failures and thus have a higher productivity than the average manufacturing firm in Ghana.

4.3 Data and Summary Statistics

The data we use in the econometric analyses is from the World Bank Regional Project on Enterprise Development (RPED) dataset (World Bank, 2008). This is a panel survey of Ghanaian manufacturing firms covering the period from 1991 to 2002 and includes the value of gross production, wage bill, number of employees, value of total raw materials, energy expenses, 4 digit industry ids, value of fixed assets, and investment among other variables. We focus on the 1998-2002 period, since data on investment climate are available only after 1997 for most of the firms. Box 1 provides more information about the data while Table A1 in the Appendix gives the definitions of all variables used in the analyses. A major limitation we face with the data is that despite the availability of information on various definitions of institutional quality and investment climate, there is a lack of information on SBRs per se. This poses a major constraint to our approach to measuring effective SBRs as explained in te Velde (2006) and Qureshi and te Velde (2007), as including an organized private sector, an organised public sector, and an institutionalized mechanism of SBR. In general, however, effective SBRs are linked to good institutions and a better investment climate. We are therefore forced to adopt indicators of the investment climate and regulatory constraints as proxies for effective SBRs.

Table 1 provides summary statistics for the variables used in subsequent regressions. Throughout, it illustrates a wide variation in firm characteristics. The average age of the surveyed firms is approximately 18 years and the average size is 68 employees; most of the firms have no foreign ownership and are non-exporting firms. Observable differences also exist in terms of the investment climate indicators – for example, while only about a fifth of firms in our sample complain that changes in government regulations have made it "harder" to do business, as many as half the sample of firms consider the aspects of the Ghanaian investment climate as "unfriendly" revealed through their responses regarding the most serious obstacles to their business operations. In terms of political networks, it appears there is substantial variation in the numbers of politicians and public officials known by firms. The number of politicians known varies from zero to 140 with a mean of about three. Similarly, the number of bureaucrats known varies between 0 and 500 with a mean of about 15.

Table 1: Summary Statistics

Variable	**Observations**	**Mean**	**Std. Dev.**	**Minimum**	**Maximum**
Total Factor Productivity	1744	658	1425	73	54951
Output	1744	2,180,000	9,480,000	50	147,000,000
Capital stock	1744	3,570,000	23,200,000	14	400,000,000
Intermediate inputs	1744	1,734	7,828	0.01	130,000
Employment	1744	68	146	1	1,800
Education of employees	1705	9.8	2.6	0	21.1
Age of employees	1705	31.3	8.2	15	61.7
Firm age	1689	18.1	12.2	0	73
Foreign	1744	0.2	0.4	0	1
Exports	1735	0.2	0.4	0	1

Union	1732	0.3	0.5	0	1
Micro size	1744	0.2	0.4	0	1
Small size	1744	0.4	0.5	0	1
Medium size	1744	0.4	0.5	0	1
Climate	1744	0.5	0.5	0	1
Overregulation	1744	0.2	0.4	0	1
No. of politicians known	714	3.5	11.0	0	140
No. of civil servants known	714	14.7	34.9	0	500

Note: Output, Capital stock and Intermediate inputs are a thousand cedis in current prices.

Tables 2a and 2b looks closely at the investment climate indicators with respect to the size of firms. It is instructive to know that micro and small firms, relative to their medium sized counterparts, are the most penalized by the adverse investment climate. About 63 percent of micro firms face serious obstacles with the business climate, compared with only a third of medium sized firms. Moreover, these micro firms are less likely to have 'friends' within government either as politicians or bureaucrats, compared with medium sized firms.

Table 2a: SBR by Firm Size

	Over-regulation		**Adverse business climate**	
	No	Yes	No	Yes
Firm size				
Micro (1-5)	82.9	17.1	37.3	62.7
Small (6-29)	82.1	17.9	43.0	60.0
Medium (30-99)	75.4	24.6	66.8	33.2
All firms	*79.5*	*20.5*	*51.7*	*48.3*

Table 2b: SBR by Firm Size

	Mean number of:	
	Civil servants known	**Politicians known**
Firm size		
Micro (1-5)	5	0
Small (6-29)	13	1
Medium (30-99)	22	4
All firms	*15*	*2*

Box 1: RPED Panel Survey

The World Bank Regional Project on Enterprise Development (RPED) survey is a comprehensive panel dataset from surveys of the Ghanaian manufacturing sector conducted in seven rounds between 1991 and 2002. The data was collected by a team from the Centre for the Study of African Economies (CSAE), University of Oxford, the University of Ghana, Legon, and the Ghana Statistical Office. The first sample of firms was drawn randomly from the Census of Manufacturing Activities conducted in 1987. The firms were categorized based on sector and location. In total, there are 9 sectors including textiles and garments and metal works. They were also categorized by location: Accra, Cape Coast, Kumasi and Takoradi, all of which constitute major industrial centres in Ghana. The coverage of this dataset is quite extensive as most of the major manufacturing sectors at the time under investigation are represented. When firms exited from the sample, they were replaced with firms of the same size category, sector, and location, so that approximately (but not exactly) 200 firms were sampled in each year. The dataset has the advantage of containing a large number of firms over a long period of time and information on many firm characteristics. One attraction of the data is that it provides another important the survey collected both perception and objective indicators of the business environment in the country. The data collected span all major investment climate topics, ranging from infrastructure and access to finance to corruption and crime. Detailed productivity information includes firm finances, costs such as labour and materials, sales, and investment. This data is well suited for probing the relationship between investment climate characteristics and firm productivity. We use all the years of data in the current study, including the most recent waves –six and seven. For more information, including details on the sampling procedure, visit http://www.csae.ox.ac.uk/.

4.4 Empirical Results

We now turn to the regressions results. In this section we discuss the results from the estimation procedure described in Section 4.2, presented in Tables 3 (and Table A1 in the Appendix). The productivity of a firm is determined by a very broad set of regressors that may explain heterogeneity of firm performance. These include firm characteristics as well as the characteristics of the external environment in which the firm operates that can affect performance. The firm characteristics that we control for are standard variables in empirical literature on firm performance and include a combination of the firm's own characteristics as well as the characteristics of its employees, sector, location and the investment climate of country in which the firm operates. Table 3 presents three different sets of estimates of the determinants of firm productivity. The first set of estimates from the baseline specification (column 1) show that all the firm, employee, and location characteristics are statistically significant and confirm our *a priori* expectations. The export status and FDI status of the firm are included in the estimations because exporters and foreign firms are generally expected to be more productive than average. The export dummy has a positive and significant impact even at the 1 per cent level. This is in line with the vast literature, which has shown that exporters are typically more productive than non-exporters (see Greenaway and Kneller, 2007, for a survey). The foreign ownership dummy, *foreign*, has a positive sign: firms with positive foreign equity participation typically perform significantly better than their purely domestic counterparts. Firms with better labour quality have relatively higher TFP, since knowledge and skills of workers may directly increase firm performance and/or indirectly act as a complement to improved technologies or organizational practices (Abowd et al. 2002).[13] As for the other regressors included in Model (1), age of employees, age of firm and unionization are all positively associated with productivity while the

[13] We use the weighted average of education of the work force in a firm as a measure of labour quality.

coefficients on micro and small sized firm dummies are negative and significant, indicating that micro and small firms are less productive, compared with medium sized firms.

The second set of estimates (column 2) controls for the investment climate in which the firms operate. Model (3) is a minor modification of specification (2). Specifically, Model (3) is a dynamic version of Model (2) with the lagged dependent variable TFP_{it-1} as a determinant of contemporaneous productivity. Due to the endogeneity of the lagged dependent variable and the possibility that some other covariates of productivity could be endogenous, we estimate Model (3) by means of the GMM-Systems estimator. Column 3 shows the results of the estimations including all the investment climate indicators. For variables considered as endogenous, we use the lagged levels of these variables dated $t-2$ and before (using all available lags) as instruments for the first-differenced equations. For the levels equations we use the lagged first-differences as instruments. The validity of the instruments is checked by the Sargan test of over-identifying restrictions. The estimated models also satisfy the absence of second-order autocorrelation of in the residuals. In all cases, the *m2* test does not indicate problems with the specification or validity of instruments.

Concerning the effect of the investment climate indicators, the results in Column 3 show that all four indicators are estimated with the expected signs: *Climate* and *Overregulation* are negatively signed, while the network variables as indicated by the numbers of politicians and civil servants known have a positive effect on TFP. *Overregulation* has a negative and statistically significant coefficient, indicating that a relative prevalence of obstacles in the business environment may hamper firm performance. By contrast, *Network-civil servants* has a positive and significant coefficient, suggesting that having strong ties with public officials are indeed important for the productivity of firms in Ghana, probably more so for firms who tend to face the severest of investment climate constraints to their operations and growth. These results indicate that firms which are overregulated as illustrated by rampant 'unfriendly' changes in government regulations pertaining to their operations have a lower level of TFP than firms which are not overregulated, while the TFP of firms with many 'friends' in government will have a higher level of TFP. Being well connected with those who make and implement government policy increases the chances of being able to lobby to overcome some of the difficulties confronting normal business enterprises, such as unnecessary red tapes, the number of procedures it takes to obtain licenses and permits and the number of days it takes to clear imported goods from the port. Given the prevalent market and government failures in many sectors, it appears making friends with government bureaucrats may represent an endogenous firm response to the difficulties in doing business in Ghana.

Table 3: Estimation Results

	1: OLS	2: OLS	3: SYS-GMM
VARIABLES	**TFP**	**TFP**	**TFP**
Lagged dependent variable			0.526***
Education of employees	0.0231***	0.0302***	0.0128***
Age of employees	0.0075***	0.0110***	0.0046***
Age of firm	0.0044***	0.0066***	0.0038***
Foreign	0.146***	0.177***	0.273***
Exporter	0.224***	0.233***	0.173***
Union	0.417***	0.336***	0.145***
Firm size (Medium omitted):			
Micro	-0.467***	-0.357***	-0.105***
Small	-0.283***	-0.183***	-0.0559***
Location of firm (Cape Coast omitted):			
Accra	0.349***	0.274***	0.128***
Kumasi	0.308***	0.330***	0.182***
Takoradi	0.355***	0.414***	0.108***
Sub-sector (Food & Beverages omitted):			
Bakery	0.0171	-0.0487	-0.0267
Garment	-0.268***	-0.468***	-0.212***
Textile	-0.0166	0.0082	-0.166***
Wood	-0.258***	-0.448***	-0.288***
Furniture	-0.200***	-0.263***	-0.0948***
Metal	-0.0397	-0.148**	-0.0186
Machines	0.0171	-0.0966	0.0421
Chemical	-0.248***	-0.263**	-0.0929
Climate		0.0090	-0.0007
Overregulation		-0.0047	-0.0940***
Network -politicians		0.0008	0.0000
Network -civil servants		0.0017***	0.0010***
Constant	5.370***	5.343***	2.482***
Year dummies	Yes	Yes	Yes
R-squared	0.55	0.60	
m2			0.40
Sargan			0.90
Observations	1633	687	611

Note:

1. *** p<0.01, ** p<0.05, * p<0.1.
2. The Sargan test is for the validity of the set of instruments.
3. The test for 2nd (m2) - order serial correlation is asymptotically distributed as standard normal variables (see Arellano and Bond, 1991). The p-values report the

probability of rejecting the null hypothesis of serial correlation, where the first differencing will induce (MA1) serial correlation if the time-varying component of the error term in levels is a serially uncorrelated disturbance.

4.4.1 Robustness Checks of the Estimates

To assess the robustness of our findings, we present an alternative specification to equation (3) by following the 'direct approach' to estimating production functions (see Fernandes, 2007; and Dovis and Milgram-Baleix, 2009). Assuming that firms anticipate the effect of the investment climate on their productivity level, the two-step approach used previously may produce some biased estimates for the investment climate measures. The reason is that if the impact of changes in government regulations or bribery on productivity has already been taken into account by the firm, then the lagged value of productivity introduced as a regressor in the two-step approach may depend on the investment climate. This introduces additional assumptions concerning the endogeneity of the variables added to the traditional inputs in the Cobb-Douglas production function (equation 2). In sum, we estimate equation (2) with the log of real output as the dependent variable and the lagged dependent variable and the SBR measures introduced as regressors. Due to the well-known endogeneity issues discussed in Section 4.2, we estimate this model using the GMM approach with the usual instruments for the endogenous regressors. The results of estimating a 'direct' model using GMM and reported in Table A1 in the Appendix do not differ qualitatively from the earlier discussion. Interestingly, the other two investment climate measures, which were previously not statistically significant, also emerge significant. Moreover, the significant coefficients of *Overregulation* and *Network-civil servants* maintain the expected signs, confirming our previous findings.

5 CONCLUSION AND POLICY IMPLICATIONS

The relationship between states and businesses in forging economic growth and development has been an enduring area of research for economists and political scientists since the Industrial Revolution of the 17th Century. The relationship between the state and business community in Ghana has varied since independence. Though each government has had distinct relations with business and private sector, civilian governments have generally promoted and enjoyed good rapport with the business community while military governments especially in the 1980s have tended to have confrontations with the private sector. This study used a multi-disciplinary approach that included both qualitative and quantitative aspects of the disciplines of political science, economics, history, sociology and organizational management. To seek to understand what constitutes effective SBR, and to assess how SBR are related to economic performance, the study relied on historical institutionalist inductive theories- comparative historical analysis and path-dependence, among others. For this analysis, the study relied on both primary data, from interviews with selected formal and informal enterprises and regulatory agencies within Ghana, and secondary data derived from a review of statutory literature such as the Constitution of Ghana, Acts of Parliament, Statutes, Codes, Contracts, rules and procedures and conventions establishing institutions. The purpose here was to examine the characteristics of formal and informal rules and regulations governing the establishment and operation of foreign and indigenous businesses, how these have evolved over time and how they may have impacted economic performance.

For the quantitative economic analysis, the study used a panel of 256 Ghanaian manufacturing firms over the period 1991-2002 to analyze the extent to which an effective SBR is beneficial to economic performance. Focusing on total factor productivity, we have found that an effective SBR or a sound investment climate correlates positively with better firm performance, possibly channelled via a more optimal allocation of resources in the economy. Concerning the effect of the investment climate indicators, our results show that an 'unfriendly' investment climate illustrated through firms' perceptions about economic and regulatory policy uncertainty affecting their operations and growth are negatively are negatively correlated with productivity, while social networks as indicated through the extent to which firms or their managers have close contacts within the government or bureaucracy have a statistically positive correlation with firm performance. These results indicate that being well connected with those who make and implement government policy increases the chances of being able to lobby to overcome some of the difficulties confronting normal business enterprises, such as the number of procedures it takes to obtain licenses and permits and the number of days it takes to clear imported goods from the port.

Narrative analysis of state agencies and PEF's perceptions of SBRs in Ghana from 1992 to 2008 which also coincides and extends beyond the period of econometric analysis of SBRs on firm performance confirms the results discussed above. Both state and BAs agree on a shift from a predominantly ad hoc and informal clientelistic relationship to a more formal and synergistic SBRs in Ghana since 1992. Formal and regularized meetings between state agencies and businesses have positively impacted on firm productivity. For instance, PEF's formal advocacy role and function resulted in the use of GCNET to expedite clearing of imported goods. Business concerns of firms are channeled more often through formal by BAs to state agencies. Firms through their BAs make inputs into budget and other policy on formalized basis. Moreover, strong formal relationship between the executive and BAs such as the investors advisory council have helped firms stay close to government and bureaucracy.

Overall, our findings contribute to understanding the link between an effective SBR and economic performance. This paper adds to the work done by Qureshi and te Velde (2007) by investigating the key determinants of firm performance and also assessing the relationship between an effective SBR and firm productivity in Ghana. The results of the study stress the need for an enabling environment for the private sector. Experiences from East and Southeast Asian economies have also shown that investment and productivity growth critically hinges on an effective and vibrant private sector underpinned by a sound investment climate. Promoting a sound investment climate is one of the core responsibilities of the state in both developed and developing countries to achieve rapid capital accumulation and sustained growth and poverty reduction. Markets are good but are not without flaws. Thus, in order for inequalities in incomes and opportunities not to be exacerbated by the markets, it is important that the many constraints that inhibit the private sector from responding effectively to market incentives are removed, complemented with an increased effectiveness of government involvement in supporting private sector activities. Apart from the positive effect of SBRs on economic performance, the other lesson which can be drawn from the paper is that even though successive governments in Ghana have shown some commitment to supporting a viable private sector that commitment has, at the same time, been undermined by governments' own fear of a strong private sector acting as a countervailing force and thereby weakening their monopoly over neo-patrimonialism. Consequently, the commitment may be seen as a public relations hoax. An effective SBR in Ghana requires sustained formalized political commitment to policies that sees the private sector as a catalyst and initiator of pro-poor growth and development.

REFERENCES

Abowd, John; John Haltiwanger; Ron Jarmin; Julia Lane; Paul Lengermann; Kristin McCue; Kevin McKinney; and Kristin Sandusky (2002) 'The Relationship between Human Capital, Productivity and Market Value: Building Up from Micro Evidence.' Paper prepared for the NBER/CRIW conference, Washington, D.C.

Adeboye, T. (1997)*'Models of Innovation and Sub-Saharan Africa's Development tragedy'*, *Technology Anaysis and Strategic Management*, Vol.9 No.2, pp. 213-235.

Adeboye, T. (1998) *Science and Technology for Africa's Development,* Paper presented at the UNECA, Addis Ababa, Ethiopia.

African Peer Review Mechanism (2005) *Country Review Report and Programme of Action of the Republic of Ghana* (Midrand, South Africa: APRM Secretariat), June.

Alavi, Hamza (1972) 'The State in Postcolonial Societies: Pakistan and Bangladesh' (New Left Review, No. 74).

Arhin, K. (2001) *Transformations in Traditional Rule in Ghana (1951-1996)* (Accra: Sedco).

Arthur, Peter (2006) 'The State, Private Sector Development, and Ghana's "Golden Age of Business"' (African Studies Review, Vol. 49, Number 1).

Aryeetey, E. (2000) A Diagnotic Study of Research and Technology Development in Ghana, Technical Publication No. 60, Institute of Statistical, Social and Economic Research, University of Ghana.

Aryeetey, E., (ed.) (2005) *Globalization, Employment and Poverty Reduction- A Case Study of Ghana*, Accra, ISSER, University of Ghana.

Asamoa, A. (1996) *Socio-Economic Development Strategies of Independent African Countries- The Ghanaian Experiance*, Accra, Ghana Universities Press.

Ayee, Joseph, Lofchie, M. and Wieland, C. (1999) "Government-Business Relations in Ghana: Experience with Consultative Mechanisms", *PSD Occasional Paper*, The World Bank, Private Sector Development Department (No. 36, October), pp. vi+64.

Ayee, Joseph R.A. (1999) "Ghana" in Ladipo Adamolekun et. al. *Public Administration in Africa: Main Issues and Selected Country Case Studies*, (Westview, Boulder, CO), Chapter 15: 250-274.

Ayee, Joseph R.A. (2008) "The Balance Sheet of Decentralization in Ghana", in Fumihiko Saito (ed.) *Foundations for Local Governance: Decentralization in Comparative Perspective*. (Leipzig: Physica-Verlag Springer, 2008), Chapter 11: 233-258.

Barzaley, M. (2001) *The New Public Management – Improving Research and Policy Dialogue*, Oxford, University of California Press.

Barzaley, M., Gallego R., From "New Institutionalism to Institutional Processualism": Advancing Kno (incomplete reference)

Berry, LaVerle (ed.) (1995) Ghana: A Country Study (Washington: Federal Research Division, Library of Congress).

Clark, G.L. and Dear, M. (1984) *State Apparatus, Structures and Language of Legitimacy* (Boston: Allen & Urwin).

Danso-Boafo, Kwaku (1996) *The Political Biography of Dr. Kofi Abrefa Busia* (Accra: Ghana Universities Press).

Dovis, Marion and Milgram-Baleix, Juliette (2009) "Trade, Tariffs and Total Factor Productivity: The Case of Spanish Firms", *The World Economy*, pp. 575-605.

Fernandes, A. M. (2007) 'Trade Policy, Trade Volumes and Plant-level Productivity in Colombian Manufacturing Industries', *Journal of International Economics*, **71**, 1, 52–71.

Ghana, Republic of (2002) *Ghana Poverty Reduction Strategy, 2003-2005* (Accra: NDPC).

Ghana, Republic of (2005) *Growth and Poverty Reduction Strategy (GPRS II), 2006-2009* (Accra: NDPC).

Ghana Statistical Service (2007) *Ghana Standard of Living Survey* (Accra: Ghana Publishing Corporation).

Greenaway, D., Kneller, R. (2007) "Firm heterogeneity, exporting and foreign direct investment." *Economic Journal*, 117, F134-F161.

Griliches, Zvi and Jacques Mairesse (1998) "Production Functions: The Search for Identification," In: Zvi Griliches (ed.) *Practicing Econometrics, Essays in Methods and Applications*, Edward Elgar, Cheltenham.

Hisahiro,K (2005) "Comparative analysis of governance, relationship between bureaucracy and policy coordination capacity with reference to Bangladesh", Japan International Cooperation Agency.

Hutchful Eboe (2002) *Ghana's Adjustment Experience: The Paradox of Reform*. (Oxford/Portsmouth/Accra: James Currey/Heinemann/Woeli Publishing).

ISSER (2007) *The State of the Ghanaian Economy in 2006* (Accra: ISSER).

Killick, Tony (1978) *Development Economics in Action: A Study of Economic Policies in Ghana* (New York: St. Martins Press).

Kingdon, John (1984) *Agenda, Alternatives, and Public Policies* (Boston: Little Brown).

MacEvan, Arthur, (1999) *Neoliberalism or Democracy? Econokic Strategy, Markets and Alternatives for the 21st Century* (London, Zed Books).

Martinusssen, John (1997) *Society, State and Market. A Guide to Competing Theories of Development* (London: Zed Books Ltd.).

Nickell, S. (1981) "Biases in Dynamic Models with Fixed Effects", *Econometrica*, vol. 49, no. 5, pp. 1417-26.

Ninsin K., and Hansen, E., (eds) (1989) *The State, Development and Politics in Ghana*, CODESRIA Book Series, London, United Kingdom.

Oquaye, Mike (1980) *Politics in Ghana*, 1972-1979 (Accra-Tema, Ghana Publishing Corporation).

Pellow, D. and Chazan, N. (1986) *Ghana: Coping with Uncertainty* (Boulder, CO.: Westview Press).

Poulantzas, Nicos (1978) *State, Power and Socialism* (London: New Left Books).

Qureshi, M. and Te Velde, D.W. (2007) 'State-Business Relations and Firm Performance in Zambia'. *IPPG Discussion Paper* No. 5.

Sen, K and te Velde, D.W. (2007)"State Business Relationships and Economic Growth in Sub Saharan Africa", *IPPG discussion paper 8*.

Tangri, Roger (1999) *The Politics of Patronage in Africa: Parastatals, Privatization and Private Enterprise* (Oxford: James Currey).

Wooldridge, J. (2002) *Econometric Analysis of Cross-Section and Panel Data* (Cambridge, MA: MIT Press).

World Bank (1997) World *Development Report 1997: The State in a Changing World* (Oxford, Oxford University Press).

APPENDIX

Table A1: Alternative Estimation Results

	Log Real Output	
VARIABLES	**Coefficient**	**Standard Error**
Lagged dependent variable	0.505***	(0.0073)
Capital stock	0.101***	(0.0147)
Employment	0.569***	(0.0268)
Education	0.0287***	(0.0051)
Age of employees	-0.00357**	(0.0015)
Age of firm	-0.00073	(0.0012)
Foreign	0.366***	(0.0876)
Exporter	0.473***	(0.0368)
Union	0.0929	(0.1010)
Firm size (Medium omitted):		
Micro	0.701***	(0.0518)
Small	0.517***	(0.0303)
Climate	-0.119***	(0.0154)
Regulation	-0.0414**	(0.0179)
Network -politicians	0.0028***	(0.0008)
Network -civil servants	0.0008***	(0.0000)
Location of firm (Cape Coast omitted):		
Accra	0.257***	(0.0415)
Kumasi	0.371***	(0.0342)
Takoradi	-0.132***	(0.0392)
Sub-sector (Food & Beverages omitted):		
Bakery	0.349***	[0.0515)
Garment	-0.403***	(0.0629)
Textile	-0.297***	(0.0910)
Wood	-0.571***	(0.0849)
Furniture	-0.390***	(0.0586)
Metal	-0.0253	(0.0633)
Machines	-0.300***	(0.1090)
Chemical	0.438***	(0.1690)
Constant	4.410***	(0.2420)
Year dummies	Yes	
m2		0.89
Sargan		0.10
Observations	613	

Notes: Same as Table 3

Table A2: List of Variables and Their Definitions - RPED Panel Data

Variable Name	Variable Description
Total Factor Productivity (TFP)	Calculated using the Levinsohn and Petrin (2003) methodology
Output	Real value of firm’s total production during previous year
Capital Stock	Real value of firm’s total capital stock
Intermediate input	Real value of firm's raw material cost
Employment	Firm's total employment level
Education	Weighted average of education of employees in the firm
Age of employees	Weighted average of age of employees in the firm
Age of firm	Firm age
Foreign	Dummy = 1 if firm has some foreign ownership
Union	Dummy = 1 if labour force is unionized
Exporter	Dummy = 1 if firm exports
Firm size (Medium omitted):	
Micro	Dummy = 1 for microenterprises (1 - 5 employees)
Small	Dummy = 1 for small firms (6 - 29 employees)
Climate	Dummy = 1 if firm reports 'Finance', 'Licensing', 'Business support', 'Infrastructure', 'Taxes', 'Labour regulation' and 'Policy uncertainty' as the most serious obstacles to operations
Overregulation	Dummy = 1 if firm reports that changes in government regulations in any of the following areas have made it harder to do business: ownership regulations, labour regulations, taxation, licensing, price controls.
Network - politicians	Number of politicians 'known' by the firm
Network - civil servants	Number of civil servants 'known' by the firm
Sub-sector dummies	A dummy for each of the following industrial sectors: Bakeries, Furniture, Garments, Textiles, Metals, Machinery, Wood Products. The omitted sector is Food Processing
Location dummies	A dummy for each of the following regions: Accra, Kumasi, Takoradi. The omitted region is Cape Coast.
Year dummies	A dummy for each of the years covered in the sample (1991-2002). The omitted year is 1991.