The Economy of Ghana Network (EGN)
Institute of Statistical Social and Economic Research (ISSER)

Policy Brief

June 30 2015, No. 5

Ghana's Fiscal Challenge and IMF Bailout

INTRODUCTION

In 2013, Ghana's hitherto encouraging economic growth was stalled by a potent cocktail of sharp falls in oil, gold and cocoa prices and acute power shortages which negatively affected productivity in both manufacturing and service sectors. Following the discovery of economic quantities of oil at the Jubilee Fields, Takoradi, Ghana was slated to make significant investments towards achieving the Millennium Development Goals (MDGs) with the estimated revenue from the sale of crude oil. Government spending increased as budget policies were reviewed to reflect higher export revenue expectations which did not materialize. The result was a wider fiscal and current account deficits, leading to rapid depreciation of the cedi and further inflationary pressures in a net importing country.

Currently, inflation, the energy crisis and the growing demand (and cost) of foreign currency in the country is estimated to have worsened, thus stifling the generation of income from which a large portion of tax revenue is deducted for use by the Ghanaian government. Export industries are equally impacted and export revenues will continue to fall if production falls, further widening the current account deficit and putting/applying, pressure on foreign exchange reserves. Additionally, with the growing debt from large deficits, Ghana is threatened by looming high indebtedness which will lower credit ratings and the market confidence of foreign and domestic investments, thus raising interest cost. Policy intervention and reform is recommended to stabilize the economy, thus ensuring a positive outlook.

The International Monetary Fund (IMF) has historically served as a partner in many of Ghana's reform initiatives. In 2014, the Ghana government once again sought the assistance of the IMF to the tune of a billion dollars in debt financing, with conditional structural change. The IMF assistance is important for two main reason. First, it is a costless balance of payment support, with 0% interest rate to be paid over ten years, compared to a market rate of 8% and secondly the IMF program is expected to encourage disciplined economic management hence giving toward credit-worthiness. However, it is stipulated that the current economic downturn may neutralize the impact of the program, making the expected macroeconomic goals unrealistic and difficult to achieve.

This Policy Brief presents findings from an assessment of the policy impact of the bailout looking specifically at the IMF terms and objectives of the bailout and also the systemic underpinnings that could potentially alter the achievement of its set goals.

KEY POLICY CONCERNS

- The projected economic targets appear unrealistic given the current weak fiscal stance, energy crisis, the continuous depreciation of the cedi and high interest rates. For example, the programme anticipates a sharp reduction in the fiscal deficit from 9.4% of GDP in 2014 to 3.7% of GDP in 2017, which, given the current culture of high expenditure, seems too drastic a behavioural shift.

- The proposal to reduce the central bank support in financing the fiscal deficit to zero over the medium term in the current circumstance may be unrealistic, since the government, in current need of deficit financing, could reach out to other sources, at significantly higher rates.

- The fund allocation for Ghana provides only 12.5% of the US$918 million facility disbursed upfront. This is a small amount relative to Kenya's allocation of 78% of a US$535 million Standby Credit Facility in February 2015. The piecemeal distribution of the fund speaks to IMF's confidence in the Ghanaian government and its ability to succeed at fiscal reform.

- The IMF instrument is considered detrimental to the state of the Ghanaian economy. The instability of the cedi and falling export values are not addressed by the restructuring terms and the conditions given by IMF could potentially slow down growth, job creation and debt reduction.

- There is lack of evidence the pressure on the cedi will abate in the long term. The weak external sector continues to show balance of payments deficits from net imports, further expanding the current account deficit and fueling high domestic interest rates and cedi depreciation which contribute to the disturbing nature of the country's debt.

CONCLUSION AND RECOMMENDATIONS

Ghana's macroeconomic performance over the 3 year period, with falling GDP growth, rising double-digit inflation and a depreciating Ghana cedi, is significantly linked to fiscal indiscipline and an unsustainable public debt to GDP ratio. The IMF programme aims to restore macroeconomic stability with a loan instrument to push development and structural reforms which are expected to lower the deficit and inflation levels that are a counteractive to GDP growth. As discussed above, the goals targeted by the programme appear lofty, given the short time frame within which the policies are to be executed. Additionally, the impact of the exchange rate has not been addressed in the fund objectives, raising further concerns that depreciation of the cedi will cause further increase in debt values, thus reversing any progress made by the bailout. Finally, the IMF support bailout is a short-run solution. The economic challenges such as the wage bill and the energy crisis should be reviewed internally and addressed in order to sustain the anticipated effects of the bailout in the long-run.

The following recommendations are made:

- Revision of fiscal targets given the structural weaknesses of the country's public finance and economic downturn.
- The Bank of Ghana should be independent of the executive arm of the government with regards to money supply, inflation and public debt.
- The Financial Administration Act (FAA) and its accompanying regulations should be amended to focus on outputs and responsibilities and expenditure control, especially in payroll management.
- Implementation of policies to encourage and expand robust internal revenue mobilization and administration,
- The country's manufacturing sector should be revived to help conserve foreign exchange and support the value of the cedi, suppress inflation and support economic growth.

Presenter:
Professor Newman Kwadwo Kusi, Executive Director of the Institute for Fiscal Studies, Accra.

The policy brief is based on a workshop on the theme "Ghana's Fiscal Challenge and the IMF Bailout" held at ISSER on 30th June, 2015. The opinions expressed do not necessarily represent the opinions of the EGN or ISSER.

Published by

The Economy of Ghana Network (www.egn.org.gh/ amafenny@yahoo.co.uk)
under the auspices of
The Institute of Statistical Social and Economic Research (ISSER)
University of Ghana, P.O. Box LG 74, Legon
Tel: +233 302 501182 / +233 302 512504
www.isser.edu.gh/ publications@isser.edu.gh

This brief is based on a workshop organized by the EGN.
Publication of this brief is funded by the ACBF