The Economy of Ghana Network (EGN)

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Policy Brief

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PUBLIC DEBT AND SUSTAINABILITY: WHITHER GHANA?

INTRODUCTION

The International Monetary Fund (IMF) introduced 50% debt to GDP ratio as the threshold within which, low income countries can continue to pursue development objectives, while keeping external debt sustainable. Using this debt sustainability framework, it assumes that, as long as a country has strong policies and institutions, it can sustain a higher level of debt. Therefore a country would be able to cover debt and interest payments with domestically generated revenue, without slowing down economic growth. Currently, Ghana's debt to GDP ratio is marked at 72.7 %, a position which is defined by the IMF's framework as "debt distress". Many contend that Ghana's present predicament is unsustainable and efforts must be made to manage and control debt.

Ghana's level of indebtedness has worsened over the years, with the public debt stock in 2015 more than twenty times that of 2006. The growth of both domestic and external debt stock from 2006 to 2012 raises a number of risks from high debt levels The overview of the trends of the public debt stock identifies the risk and benefits of the different financing instruments, and the policies that balance their impact on the economic growth, future debt service and vulnerability to macroeconomic shocks. Prudent debt management through maintaining fiscal responsibility, balancing the choice of financing sources and instruments and reducing the share of public debt valued in foreign currency. This will minimize the country's vulnerability to external shocks.

Key issues raised:

- **Ghana's Public Debt:**

  Both domestic and external debt accounted from Ghana's worsened indebtedness was attributed to the increased medium term investments, the US$780 million Eurobond contracted at the end of 2007 and the nearly US$ 1 billion IMF Extended Credit Facility approved in 2015. By 2015, External debt had overtaken Domestic debt as the major source of public financing.

  By 2008, the government operated at a 14.5% fiscal deficit, financed by increased external borrowing. Balance of payment pressures caused rapid currency depreciation as the Ghana Cedi performed progressively worse alongside the main currencies the loans were valued in, the Euro, the US Dollar and the Special Drawing Rights (SDR). Resulting in the revaluation of loans and debt service leading to a further increase in the public debt stock (Table 1).

Table 1

	Total Domestic Debt	Share of Total Debt	Total External debt	Share of Total Debt
2006	2.9	59.2	2	40.8
2015 (June)	35.9	38	58.6	62

Implication

- Huge debt service requirements to cover principle and interest payments in the future. It is worth noting that total debt service as a percentage of GDP increased from 20% in 2009 to 79% in 2014.
- Increased vulnerability to macroeconomic shock, affecting the stability and growth, making it even more difficult to manage.
- Historically, government spending is known to increase in election years. Despite the need for fiscal consolidation to curb the deficit and further borrowing, we may face a worsening budget deficit in the upcoming election year.
- Weakening investor confidence in Ghana because of the lingering doubts about long-term macroeconomic stability and fiscal sustainability.

Conclusion and Policy Recommendations

Ghana's most recent attempt at realising goals for the debt and fiscal sustainability is in the form of a debt management strategy adopted in 2009. The government, under this strategy, sought to avoid borrowing in foreign currency, ensure accountability of all market-related foreign financing through close-monitoring and data collection and increase management capacity through the formation of guidelines and training on monitoring and risk-management. Having surpassed the threshold for sustainability, it is crucial that policy and efforts to manage and reduce debt are introduced for the sake of economic growth and the welfare of future generations.

The following debt management strategies are recommended:

- Avoiding non-concessional borrowing in foreign currency
- Evaluating projects on a case by case basis to establish economic return, impact on debt sustainability, and alternatives.
- Broadening of investor base
- Issuing fixed-rate long-term bonds in domestic currency
- Ensuring that all funds raised through debt are invested in projects with high private or social return.

Presenter:

Professor Newman Kwadwo Kusi, the Executive Director of the Institute for Fiscal Studies, Ghana.

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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/info@isser.edu.gh

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