The Debt Sustainability Analyses (DSA)

The IMF and World Bank regularly conduct joint debt sustainability analyses (DSAs) for low-income member countries based on their agreed Debt Sustainability Framework (DSF). The analyses examine the projected trajectories of debt levels and other macroeconomic variables over some twenty years. DSAs were initially focused on the sustainability of external debt, but now give similar weight to assessing overall domestic and external public sector debt sustainability. The DSF was introduced in April 2005 to help guide countries and donors in mobilizing the financing of low-income countries' development needs, while reducing the chances of an excessive build-up of debt in the future.

The latest DSA places Ghana at a high risk of external debt distress. This was on account of the debt service-to-revenue ratio which exceeds the high performer threshold of 22 per cent. All the other indicators "would remain below their CPIA (to be explained below) dependent thresholds by <u>comfortable margins</u> under the baseline". Overall debt vulnerabilities have increased since the last DSA (Article IV Consultation Report April 2014) where the risk of debt distress was assessed as moderate.

The latest DSA uses the <u>residency criterion</u> for defining external debt. This is meant to better capture domestic debt held by non-residents. "Due to the change of the criterion for external debt, debt service increased to some extent, leading to a worsening of debt-service related indicators". The debt outlook is particularly sensitive to shocks to nominal exchange rate and net non-debt creating flows. "The use of the currency criterion (as in the previous DSA) would not change the risk of debt distress".

This DSA also incorporates non-government-guaranteed external debt contracted by SoEs. The use of the residency criterion partly masks SoE's vulnerabilities associated with their large foreign currency-denominated liabilities from resident banks.

The debt-to- GDP ratio is on an increasingly risky path and will require persistent fiscal consolidation and deceleration in exchange rate depreciation to stabilize it. This puts Ghana's medium term prospects at risk.

- Dollar denominated short-term obligations (large central bank swap operations) have recently been rolled over on a continuous basis, which creates additional risk to debt sustainability.
- The holdings of domestic debt instruments by non-residents present roll-over and foreign exchange risks caused by accompanying capital outflows.

The World Bank also uses its Country Policy and Institutional Assessment (CPIA) tool – a diagnostic tool that is intended to capture the quality of a country's policies and institutional arrangements—i.e., its focus is on the key elements that are within the country's control, rather than on outcomes (such as growth rates) that are influenced by elements outside the country's control. The CPIA ratings help the World Bank to determine the relative sizes of its concessional lending and grants to low-income countries (IDA eligibility). It also helps to guide its interventions, its assessments of risk, and its research.

The World Bank's Country Policy and Institutional Assessment (CPIA) classifies Ghana among the list of strong performers with an average score of 3.79 over the 2011 -13 period. This is marginally above the threshold for a high performance of 3.75. Deterioration in Ghana's CPIA score below 3.75 would therefore worsen the assessment of risk of debt distress because the debt burden thresholds for key indicators would be lower than at present. Weakening government commitment to reforms and policy slippages resulted in an "uninterrupted decline in CPIA scores since 2011 over the 2013 period (see World Bank report No. 95284 of June 2015, paragraph 47).

The debt dilemma poses as a great risk to the success of the program as the 2016 election approaches. It is for this reason that the program framework with the fund, seeks to ensure that GoG commits to prudent borrowing policy as one of the policies that will compliment fiscal consolidation in order to restore debt sustainability.Supported by the program loan of US $ 150 million, the Policy Base Guarantee (PBG), and a successful implementation of the ECF program, Ghana's external financing requirements is seen to remain manageable. Ghana could return to being at moderate risk of external debt distress.