<u>Second Review of Ghana's Three-Year Financial and Economic Program under the IMF Extended Credit Facility, 2015-2017</u>

A. Introduction and Background

The performance criteria and indicative targets are set for end-April, end-August, and end-December 2015. To this end CEPA has successfully conducted its own assessment of the Program for end-April and seeks to do same for end-August through this medium.

On the 31st of August 2015, the Executive Board of the International Monetary Fund (IMF) completed the first review of Ghana's economic performance under the program supported by an Extended Credit Facility (ECF) arrangement and disbursed about US$ 116.6 million bringing total disbursement under the arrangement to US$ 233.1 million.

The Executive Board granted Ghana waivers for the non-observance of the performance criteria regarding gross credit to government, and non-accumulation of external arrears. They also approved the authorities' request for modifications of the performance criteria. They welcomed the government's medium-term debt management strategy as key in reducing near-term financing risks. However they advised the government to complement its strategy by striving to deepen the domestic market, as well as by seeking to borrow externally on concessional terms as much as possible. In other to control inflation, the Board indicated that;

> "*The monetary policy stance will have to remain tight to help bring inflation down against the background of exchange rate volatility. The Bank of Ghana (BoG) should stand ready to tighten monetary policy further if inflationary pressures do not recede as expected*".

After the first review, most of the quantitative performance criteria (PC) and structural benchmarks for the remainder of the year remained unchanged. The following revisions were made:

- The PC on gross credit to the government by BoG for August and December was increased by GH₵ 1.2 billion, in view of the upward revision to the outstanding stock at end-2014 to include large overdrafts accumulated in 2014 in the form of negative deposits – these negative deposits were mistakenly excluded from the end-2014 stock of gross credit to government.
- The PC on net international reserves and net domestic assets at end-December was revised upwards by US$ 500 million and downward by GH₵ 1,504 million respectively, to reflect the larger amount of Eurobond envisioned this year.
- The indicative target for inflation was revised upward for end-August to account for the higher inflation trend observed up to June 2015 (see IMF Country Report No. 15/245, September 2015, page 58 paragraph 83).

CEPA's assessment is shown in the table below

Quantitative Program Targets

	2014	Apr-15		Aug-15				Dec-15
	Dec Act.	Apr Prog.	Apr Prov.	Aug Prog.	Aug Prov.	Δ(Prov -Prog)	Status	Dec Prog.
I. Quantitative Performance Criteria								
Primary fiscal balance of the government (floor in millions of cedis)	(3,555)	(515)	(830)	(380)	(646)	(266)	x	(422)
Wage bill (ceiling; in millions of cedis)	9,449	3,413	3,341	6,857	6,815	(42)	✓	10,286
Net international reserves of the Bank of Ghana (floor; millions U. S. dollars)	1,415	1,042	1,186	147	566	419	✓	2,278
Net domestic assets of Bank of Ghana (ceiling; millions of cedis)	3,095	5,755	4,794	8,772	7,180	(1,592)	✓	3,410
Net change in stock of arrears (ceiling; millions of cedis)	428	(643)	233	(1,001)	(623)	378	x	(1,561)
II. Continuous Performance Criteria								
Gross financing of BoG to the Government and SOEs (ceiling; in millions of cedis)	19,723	14,614	14,568	15,814	15,016	(798)	✓	15,814
Non-accumulation of external arrears (ceiling; millions of U.S. dollars)				-	-	-	✓	
Non-accumulation of domestic arrears (ceiling; millions of cedis)			797	-	902	88	x	
Contracting or guaranteeing of new external non-concessional debt (ceiling; millions U.S. dollars)				-	-	-	✓	2,500
III. Indicative Target								
Program central target rate of inflation (12 month percentage change)	17.0	15.4	16.8	15.0	17.3	2.3	x	12.0
Contracting or guaranteeing of new external concessional debt (ceiling; millions U. S. dollars)	-	-	-	-	-	-	✓	100
Social Protection (floor, in millions of cedis)	947	388	252	806	954	148	✓	1,294

Source: IMF, GOG, BOG and CEPA staff estimates

B. Assessment

1. Quantitative Performance Criteria

The quantitative performance criteria under the quantitative program targets are: a floor on the primary cash fiscal balance of the government, a ceiling on gross credit to government by the bank of Ghana, a floor on the net international reserves of the Bank of Ghana, a ceiling on net domestic assets of the Bank of Ghana, a ceiling on wages and salaries and a ceiling on the net change in the stock of domestic arrears.

1.1 Primary fiscal balance

The floor for end-August is a deficit of GH₵ 380 million consistent with Table 1 in the MEFP of the program. Table 1 below shows a surplus provisional outturn for the primary balance of GH₵ 236 million indicating an over-achievement of the target floor. The review period according to CEPA recorded a financing shortfall of GH₵ 740 million.

Donor support has been unlocked since the approval of the program. According to the Fund, the EU has released about US$ 180 million in project grants and project loans and the financing mix for the remainder of the year will be externally oriented. In all loan disbursements of US$ 1.2 billion are expected during the remainder of the year. The stunning over performance of project loan disbursement is evidence to this effect.

Table 1: Financing of the deficit (Jan-Aug 2015)

	Jan-Aug (2015)		
	Prog.	**Prov. Outturn**	**Prov-Prog**
Financing	6,338	5,598	(740)
Foreign (net)	1,166	2,278	1,112
Borrowing	2,649	3,799	1,150
Project Loans	1,901	3,187	1,286
Programme Loans	748	612	(136)
Sovereign Bond	-	-	-
Amortisation (due)	(1,483)	(1,521)	(38)
Domestic (net)	5,172	3,320	(1,852)
Banking	2,407	1,264	(1,143)
Bank of Ghana	1,658	662	(996)
Comm. Banks	749	602	(147)
Non-banks	2,685	2,050	(635)
Other Domestic Financing	80	6	(74)
Transfer to Ghana Petroleum Funds	(69)	(64)	5
Transfer from Stabilisation Fund	206	206	-
Other Domestic Financing	(57)	(136)	(79)
Memorandum Items			
OBB (financing basis)	(6,338)	(5,598)	740
Interest Payments	(6,011)	(5,834)	177
Primary Balance (- =deficit)	(327)	236	563

Source: IMF, BoG and CEPA staff estimates

However substantial delayed payments in areas CEPA referred to as the 'usual suspects' in the earlier publication makes the primary balance estimate of GH 236 million illusory. Delay payments estimated by CEPA over the review period amount to GH₵ 902 million (including domestic financed capital) which leads to the primary balance breaching its target floor by some GH₵ 266 million (see table on Quantitative Program Targets).

1.2 Wage bill

The ceiling for the review period of GH₵ 6,857 million was not breached as a saving of GH₵ 785 million was made (see Quantitative Program Target).

On the back of a World Bank study that most public sector workers in developing countries have no bank accounts insinuating the presence of "ghost workers", The study however noted: though the number of employees without bank account cannot be taken as an estimate of ghost workers in Ghana, as there are low levels of banking penetration as well as inefficient and expensive banking services levels.

To this end salaries of 47,186 employees without bank account were suspended in October and November 2014. By February 2015, 44,496 employees had been validated by the Auditor General and payments reactivated. The names of the remaining 2,690 were submitted to the Bureau of National Investigation (BNI) for investigations (see page 52 paragraph 59) without finding so far any law infraction.

Also 27,805 employees with no social security numbers were suspended in June pending regularization by September before transferring their names to the BNI for investigations. Recent developments on the labour front show that, most public sector workers' wage are in arrears and this is in contrary to the efforts of the Controller and Accountant General's Department in identifying them as ghost workers. Though CEPA may see this as delay payment, there is urgent need to ensure such payments are made before they become arrears.

1.3 Net International Reserves of the Bank of Ghana

The floor on the NIR of the BoG was reviewed downwards from US$ 331 million to US$ 147 million – a difference of US$ 187 million – to reflect the larger amount of Eurobond envisaged for this year. The target floor for the review period was over achieved by some US$ 419 million. This means the floor was observed.

1.4 Net domestic assets of Bank of Ghana

The provisional outturn for the review period of GH₵ 7,180 million is below the ceiling of GH₵ 8,772 million. CEPA assesses the target to have been achieved.

1.5 Net change in stock of arrears

The end-2014 stock of arrears was revised upward. This led to an upward revision in the 2014 fiscal cash deficit from 9.4 per cent to 10.2 per cent of GDP, as new arrears were discovered in audits of the outstanding claims from the bulk oil importers (BDCs) and a reconciliation of cross debt with the utility companies, resulting in net additional arrears of the government to the electricity company. This has led to the arrears clearance strategy to be revised. To this end data from the government website estimates a new reduction in the net change in stock of arrears target of GH₵ 1,505 million compared to the program target reduction of GH₵ 1,001 million.

CEPA maintains the program target of GH₵ 1,001 million with the assumption that entire GH₵ 687 million owed the BDCs will be cleared in 2015 using the BoG's unplanned dividends to government. We estimate a provisional outturn reduction of GH₵ 623 million - GH₵ 378 million below the target ceiling of GH₵ 1,001 million.

Table 2: Net Change in Stock of Arrears

	Jan-Aug (2015)		
	Prog.	**Prov.**	**Prov-Prog**
Arrears Clearance gross	**(1,505)**	**(1,525)**	**(20)**
Road Arrears	(272)	(119)	154
Non-Road Arrears	(1,233)	(1,407)	(174)
New Arrears	**-**	**902**	**902**
Wages & Salaries	6,857	6,815	(42)
Pensions and Gratuities	609	555	(54)
Social Security	700	556	(144)
Education Trust Fund	554	507	(47)
Dist. Ass. Common Fund	950	735	(215)
Social Benefits	59	-	(59)
Domestic Financed	866	525	(341)
Net Change in Stock of Arrears	**(1,505)**	**(623)**	**882**

Source: IMF, BoG and CEPA staff estimates

2. Continuous Performance Criteria

This comprises of four targets; gross financing of BoG to the government and SOEs, non-accumulation of both domestic and external arrears and contracting or guaranteeing of new external non-concessional debt.

2.1 Gross financing of BoG to the Government and SOEs

The ceiling was revised from GH₵ 14,614 million to GH₵ 15,814 million – an increase of GH₵ 1.2 billion – in view of the upward revision to the outstanding stock at end-2014 of some GH₵ 6.1 billion to include large overdrafts accumulated in 2014 in the form of negative deposits. This is to allow the restoring of some cash buffers, which were largely used to repay part of the 2014 overdrafts and bring gross credit to government close to the PC level at end-April 2015.

The provisional outturn of GH₵ 15,016 million was below the ceiling of GH₵ 15,814 million by some GH₵ 798 million indicating an overachievement.

2.2 Non-accumulation of external arrears

In August 2015 the staff received new information on the non-observance of the PC on the non-accumulation of external arrears. Small payments, not exceeding US$ 2 million, were due to a Spanish creditor and not paid on time since the program was approved on April 3, 2015. Other very small overdue payments were notified in mid-August and paid by August 25.

The staff clarified that any delay in payment made beyond the due date gives rise to arrears and constitutes a non-observance of the continuous PC. As a result CEPA assesses this continuous performance criterion to have been observed.

2.3 Non-accumulation of domestic arrears

CEPA estimates GH₵ 902 million of new domestic arrears accumulation (delayed payment) over the review period – this is shown in Table 2 above. The program with the Fund does not tolerate the accumulation of new arrears and as a result any arrears identified will have to be included in the arrears clearance strategy implying a larger clearance.

2.4 Contracting or guaranteeing of new external non-concessional debt

The debt limit on non-concessional loans for the remainder of 2015 has been revised upward from US$ 1,000 million to US$ 2,500 million to accommodate for a larger Eurobond issuance of up to US$ 1,500 million of which US$ 1,000 million benefits from a partial guarantee from the World Bank.

Available information will say the target of no contracting or guaranteeing of new external non-concessional debt was achieved over the review period. The US$ 2,500 million target for the year has been programmed for the later part of the year.

3. Indicative Targets

This comprises of three items; a twelve month rate of consumer price inflation, a floor on poverty-reducing government expenditure (Social Protection) and a ceiling on the contracting or guaranteeing of new external concessional debt.

3.1 Program central target rate of inflation

On account of the higher inflation trend observed up to June 2015, the indicative target for inflation was revised upward for end-August from 13.8 to 15.0 per cent. The realized figure for August according to the Statistical Service of Ghana was 17.3 per cent. The indicated target was missed.

CEPA maintains that developments in respect of the exchange rate, administered prices in respect of utilities (electricity and water) and petroleum products (transport and haulage fares) have made the modelling of inflation difficult.

With an impending major utility tariff review (initially expected in October 2015) the annual (y/y) target of 12 per cent is unlikely to be achieved. CEPA projects an end-year outcome of 17.8 per cent (y/y) and an average of 17.2 per cent (y/y).

3.2 Contracting or guaranteeing of new external concessional debt

An indicative ceiling of US$ 100 million on concessional loans has been put in place. Available information will say the target of no contracting or guaranteeing of new external non-concessional debt was achieved over the review period.

3.3 Social Protection

The target floor for the review period was over achieved by some GH₵ 148 million.

C. Conclusion

CEPA's revised assessment – on both reviews – however leads to the conclusion that the fiscal consolidation process needs to be strengthened. Also the perennial problems with arrears (delayed payments), including lack of transparency leading to discoveries of unrevealed payment arrears and delayed payments, still remain (see Table 3).

Both the CEPA and IMF position could be said to be matters of interpretation. On the other hand the data points to delayed payments and insufficient clearance of arrears as targeted – public discussions will confirm – also reforms agreed in the program are still on-going and in principle must be allowed to run their courses. For example payroll irregularities have been alluded to; inflexibilities and earmarking of revenues for statutory funds according to the Fund staff continue to reduce budgetary flexibilities (IMF Press Release No. 15/496, November 5, 2015).

Table 3: Differences – IMF and CEPA

	Apr-15			Aug-15		
	Prog	Prov.		Prog.	Prov	
		IMF	CEPA		IMF	CEPA
Primary fiscal balance of the government (floor in millions of cedis)	(515)	46	(830)	(380)	n/a	(646)
Non-accumulation of domestic arrears (ceiling; millions of cedis)	-	-	797	-	n/a	902
Net change in stock of arrears (ceiling; millions of cedis)	(424)	(565)	233	(1,001)	n/a	(623)

Ghana now faces a high level of public debt and financing constraints signalled by rising borrowing cost on both domestic and external markets. Consequently the efficient utilisation of scarce resources must be demanded. In these circumstances it is conceivable that waivers could be granted by the Fund upon satisfactory explanation by government for otherwise breaches of the performance criteria.

The CEPA assessments also suggest that the cooperation and collaboration between the fiscal authority (MOFEP) and the monetary authority (BoG) is less than required. A-go-it alone by the BoG (fiscal intransigence) is likely to result in the build-up of the requisite international reserve target but with an abandonment of the inflation target. This will manifest itself in continued real depreciation of the exchange rate and high inflation. Current developments suggest that this may very well be what is happening.