AN ASSESSMENT OF THE ECF-SUPPORTED PROGRAM WITH THE FUND: EXTERNAL TRADE AND BALANCE OF PAYMENTS

APRIL 2015 – APRIL 2016

1.0 INTRODUCTION AND BACKGROUND

After having faced two continuous years of large twin (fiscal and current account) deficits with thin external buffers, increasing depreciation pressures on the domestic currency and serious financing difficulties in 2013 and 2014, the Government of Ghana (GoG) initiated and entered into negotiations with the International Monetary Fund (IMF) from about the third quarter of 2014 for an economic reform program that could be supported by the Fund. The primary purpose was to regain policy credibility and stabilize the economy.

In early-April 2015, the Executive Board of the IMF approved a US$918 million three-year Extended Credit Facility (ECF) arrangement to support the country's economic reform program. The ECF-supported Program aimed at restoring debt sustainability and macroeconomic stability in order to foster a return to high growth and job creation.

Coming along with the Program were critical guideposts for achieving external sustainability including:

- improving the merchandise trade and current account deficits *to more sustainable levels* — i.e., around 3 percent of GDP and 5 percent of GDP respectively — by 2017;
- narrowing the overall balance of payments (BOP) deficit with the goal of achieving *surpluses in the medium term*;
- building international reserves as external buffers to cushion adverse exogenous shocks — with the *gross and net reserves cover rising to the equivalent of 4 months and 3½ months of imports of goods and services* in the medium term; and
- the BoG moving away from swap and bridging loan facilities, which have typically been used as 'window dressing' to shore up the gross international reserves (GIR).

In addition to these, a *floor has been set on the net international reserves* (NIR) of the Bank of Ghana, while *ceilings are placed on non-accumulation of external arrears and contracting and/or guaranteeing of new external debt*.

This brief note is CEPA's assessment of performance in respect of the external trade and payments for 2015 and the policy implications going forward.

The focus of the assessment is in three areas:

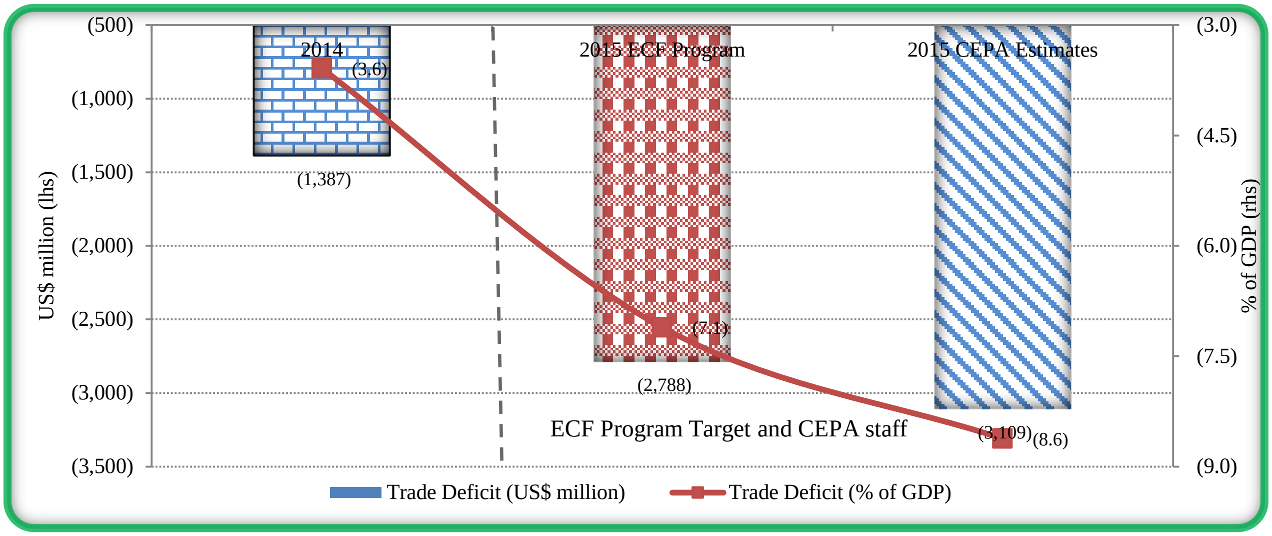
1. an examination of the merchandise trade balance in the face of continuing commodity price declines in global markets;
2. the current account deficit and its financing in the near term; and
3. a scrutiny of the overall balance of payments (BOP) deficit in the context of effective management of international reserves.

2.0 SUMMARY OF FINDINGS

2.1 Merchandise Trade Accounts

Relative to official data for end-2015, the Program target for the merchandise trade deficit appeared rather optimistic. CEPA estimates a merchandise trade deficit of US$3.1 billion, which is some US$321 million more than the program target of US$2.8 billion [see Chart 1].

Chart 1: Merchandise Trade Deficit (US$ million & % of GDP)



Data sources: IMF country Report No. 16/16, January 2016 and CEPA staff estimates

The larger merchandise trade deficit estimated by CEPA is on account of a combination of poor export outcomes and a slightly lower import bill than envisaged in the Program for 2015. The poor export outcomes reflected domestic supply-side production shortfalls and declining realized prices on world markets of major export commodities (gold, cocoa beans, and crude oil).

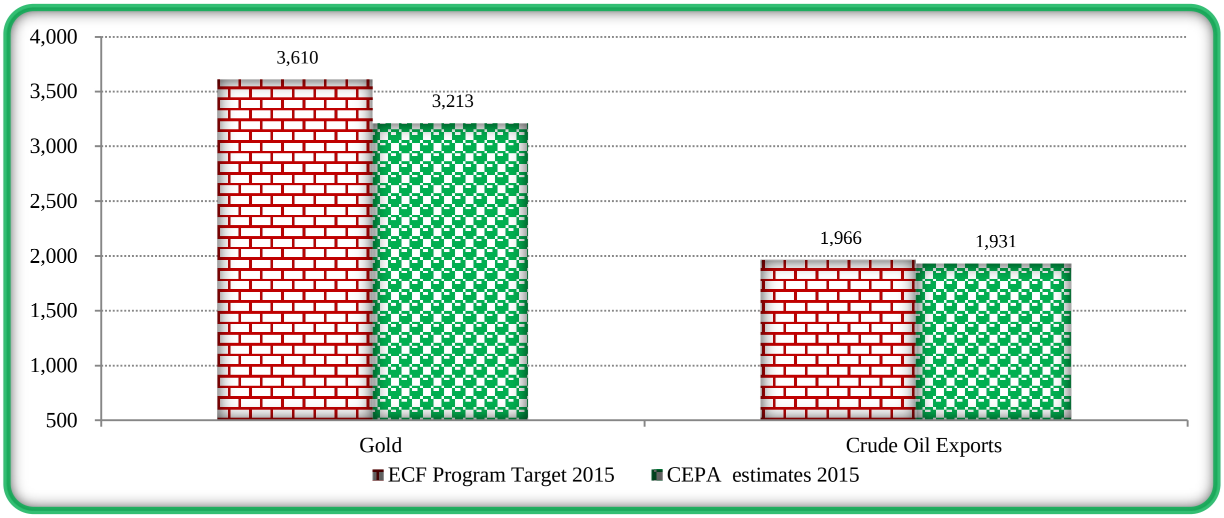
2.1.1 Merchandise Exports

Exports are estimated by CEPA to be lower by some US$655 million while imports are lower by US$334 million relative to the program target.

Relative to the Program, much reduced earnings are estimated for gold and crude oil exports by CEPA. Export receipts from gold as estimated by CEPA are some US$397 million less than in the Program on account both lower export volumes and reduced realized prices. The volume of gold exports is estimated by CEPA at 2.769 million ounces by the close of the year — which would mean a volume loss of 2.1 percent relative to the 2.828 million fine ounces anticipated in the Program. Meanwhile the spot price of gold resolutely fell below the WEO average price of US$1,277 per ounce assumed in the Program. CEPA estimates that by the close of the year the unit price per ounce could reach US$1,160, implying a price loss of some 9.1 percent relative to that of the Program.

Earnings from the exports of crude oil are also estimated to fall marginally below the target set in the Program, reflecting slightly reduced export volumes than anticipated in the Program. CEPA estimates export receipts from the shipment of crude oil from Ghana to amount to US$1,931 million based on the assumption of export volumes of 36.9 million barrels by the close of the year — some 0.9 percent lower than the 37.24 million barrels anticipated in the Program.

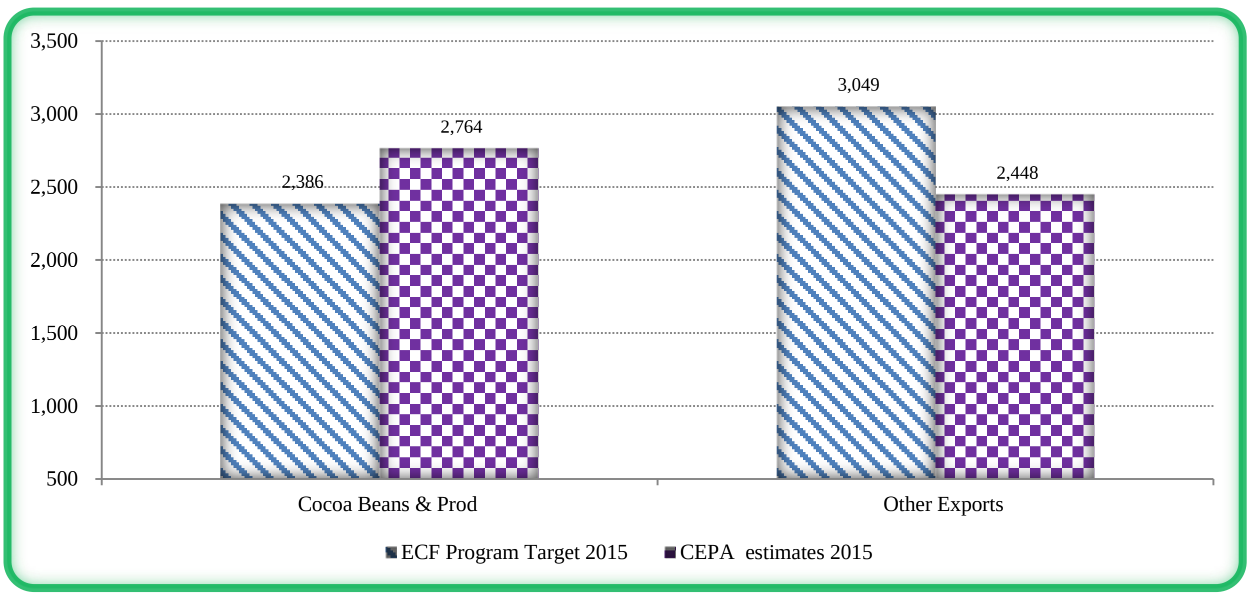
Chart 2: Gold and Crude Oil Export Receipts (US$ million)



Data sources: IMF Country Report No. 16/16, January 2016 and CEPA staff estimates

The CEPA export earnings on crude oil are some US$35 million lower than anticipated in the Program. As in the case of gold, this is also because of an anticipated marginal decrease in the average price per barrel by almost 0.9 percent below the WEO average price of US$52.8/bbl assumed in the Program.

Chart 3: Export Earnings from Cocoa Beans and Products and Other Exports (US$ million)



Our end-year estimates for 2015 also take into account the dismal performance of non-traditional exports (NTEs) over the past six years. The records show that in spite of NTEs having gained some prominence over time, its share in overall export earnings has shrunk, on average from 18 percent in 2009 to 14 percent by end-2014. This may not fundamentally change in the foreseeable future. Other export earnings (including from NTEs) are therefore projected by CEPA to amount to US$2.4 billion at the end of 2015 — some US$600 million less than anticipated in the Program [see Chart 3].

In the case of cocoa, it would be recalled that global cocoa markets witnessed a phenomenal rally in the spot price of cocoa beans from about US$2,750 per metric ton since the beginning of the second quarter of 2015; by mid-May it had overshot the WEO forecast price per ton of US$2,995 used in the Program to reach US$3,345 by end-December 2015 — far beyond what the Program had anticipated for the year.

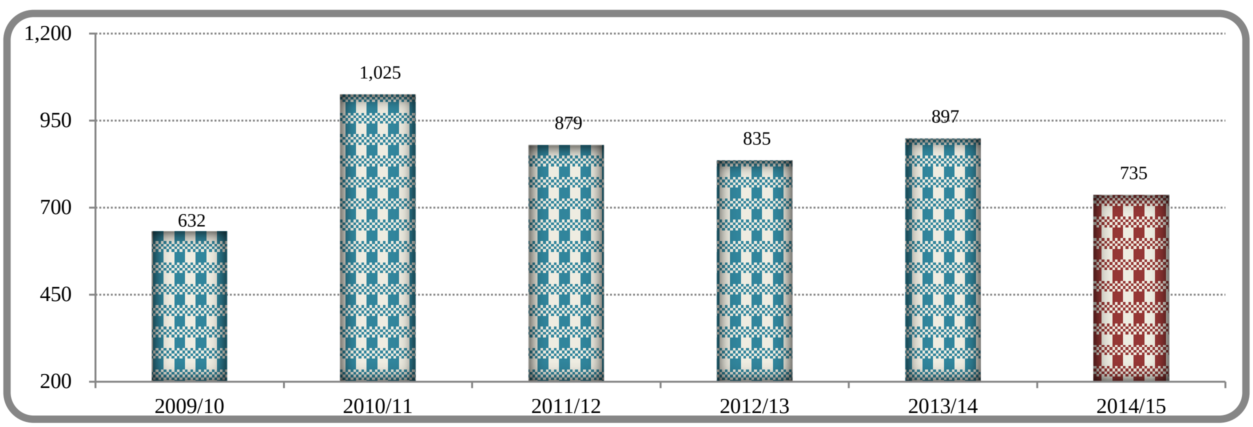
In spite of the rally in cocoa prices, Ghana experienced a sharp fall in its cocoa purchases, from about 897 thousand metric tons in the 2013/14 season to 735 thousand metric tons in 2014/15 following a very poor main crop. Export volumes of cocoa beans are therefore estimated by CEPA to be lower than anticipated in the Program because of reported poor crop purchases in the 2014/15 cocoa season.

Nonetheless, export receipts from Cocoa Beans and Products are singled out in the CEPA estimates with an outcome that is above those anticipated in the Program for end-2015. The CEPA projection of US$2.8 billion is US$378 million more than the target amount in the Program and is principally based on the positive price developments of cocoa beans on world markets [see Chart 3].

Official sources have blamed the poor ‘output’ of cocoa beans in recent years on a number of factors, including:

- harsh weather conditions (dry and prolonged Harmattan) at the start of the season;
- poor agronomic practices — specifically, *late application of pesticides and fungicides to protect cocoa trees from diseases and pests;* and
- smuggling to neighboring La Cote d’Ivoire *as a result of the depreciation of the cedi against the CFA which had eroded the value of the high producer price set at the start of the season*.

Chart 4: Cocoa Bean Purchases in Ghana (000 metric tons)



Data sources: Based on data obtained from the ICCO website and Cocobod

Statistical information from the International Cocoa Organization (ICCO) confirms, however, that ever since the historic one million metric tons was registered in the 2010/11 season, cocoa purchases in Ghana have generally been on a declining trend path with annual growth rates persistently below both the Ivorian and African average — signaling serious ‘production’ challenges in Ghana.

The historic purchase of some 1.1 million metric tons registered in the 2010/11 season was attributed to conducive weather conditions; increased fertilizer applications; improved disease and pest control; as well as increased yields from hybrid plantings. Nevertheless, Ghana reportedly gained some 205 thousand metric tons from smuggling from La cote d’Ivoire in the midst of the political crisis in that country — what CEPA refers to as the ‘Gbagbo effect’.

There are also suggestions that the Ghanaian cocoa regulatory authority — Ghana Cocoa Marketing Board (Cocobod) — has continuously had hitches with its producer-price setting and is yet to tackle an unending problem of cross-border smuggling of cocoa beans to neighboring West African producing countries. In addition, Cocobod has to adequately cope with the potential impact of a new minimum price guarantee recently launched in La Cote d’Ivoire to make farmers in that country less vulnerable to daily price fluctuations in international markets

Supply-side Implications for Economic Growth

Our overall assessment of the supply-side of the merchandise trade account is that despite efforts at diversifying the export base and raising the sophistication and value-addition in the production and exports of processed agricultural goods, the economy remains vulnerable to commodity price shocks, domestic production conditions, and the vagaries of the weather. The most recent collapse in the prices of crude oil and gold on global commodity markets has not only damaged prospects for increased economic growth, it also reduced export revenues.

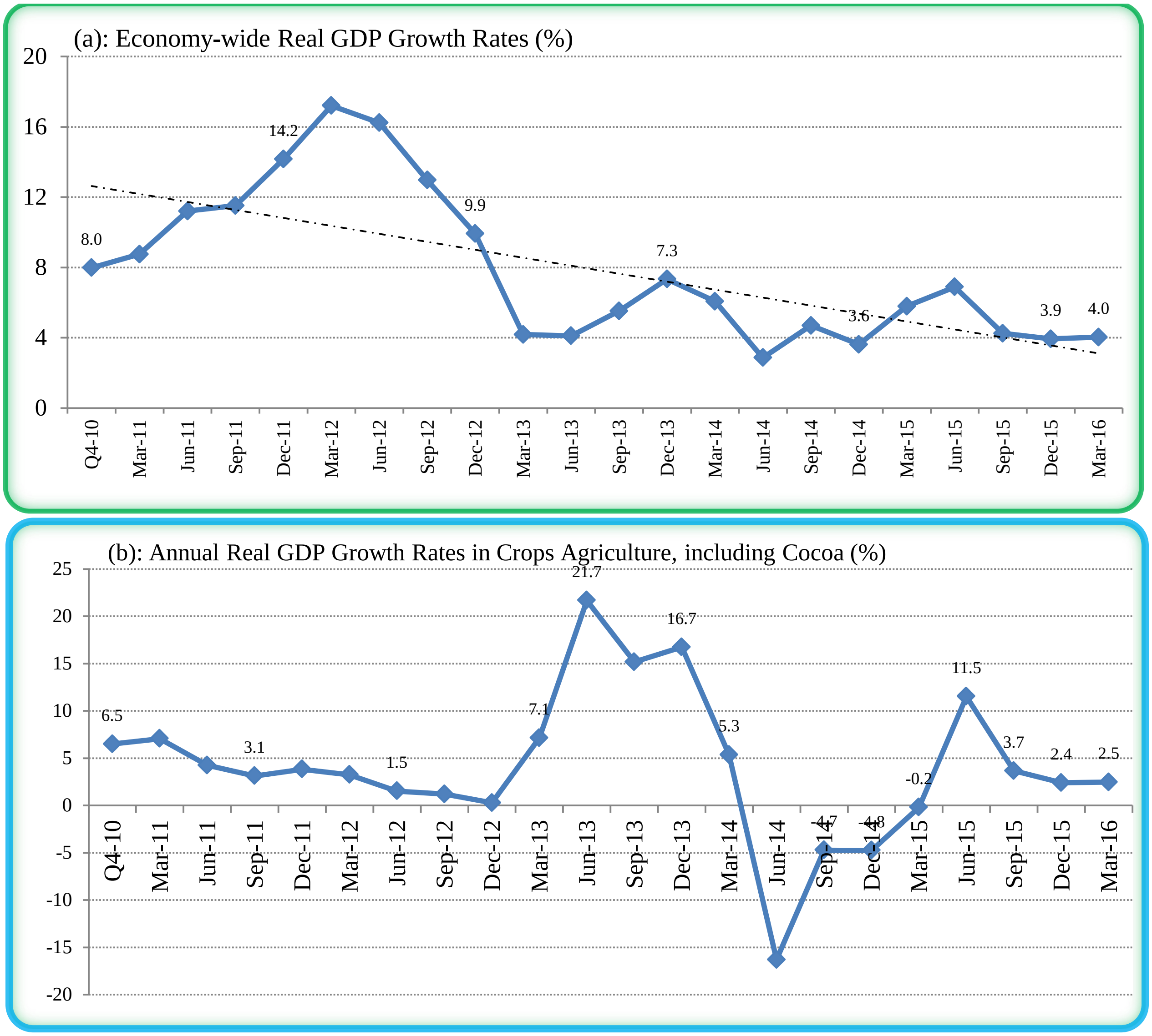
The important point that must be stressed about the low and poor export volumes of the country’s main export commodities is their direct relationship to domestic production conditions, particularly in the extractive mining and quarrying (M&Q) industries of crude oil and gold production. Annual growth rates in the overall economy have generally trended downwards, reflecting the declining growth paths of particularly the M&Q sub-sector of Industry and crops agriculture (including cocoa).

Charts 5 and 6 depict seasonally-adjusted annual real GDP growth rates for selected sectors and sub-sectors of the national economy in two separate panels each:

- the economy-wide real GDP growth rates and those for the agricultural sector, including cocoa; and
- real GDP growth rates for the M&Q extractive industries’ sub-sector of Industry and the real GDP growth rates originating from oil production.

Panel (a) of Chart 5 shows that growth in the overall economy after the dramatic spurt in 2011 — resulting from the significant extraction of crude oil from the Jubilee Oil fields — has been on a generally declining growth path: Overall real GDP growth shot up from 8% in December 2010, driven in large part by a combination of the spurt in oil production (Jubilee effect) and the so-called 'Gbagbo effect'. In subsequent years, the overall real GDP growth rate followed a declining trend path reaching 7.3% by end-2013 before decelerating sharply to an estimated 3.9% by end-2015. The sharp deceleration was on account of the negative impact of the currency depreciation on imported input costs, declining domestic demand, and increasing power outages.

Chart 5: Seasonally-Adjusted Real GDP Growth Rates in the Economy and Agricultural Sector



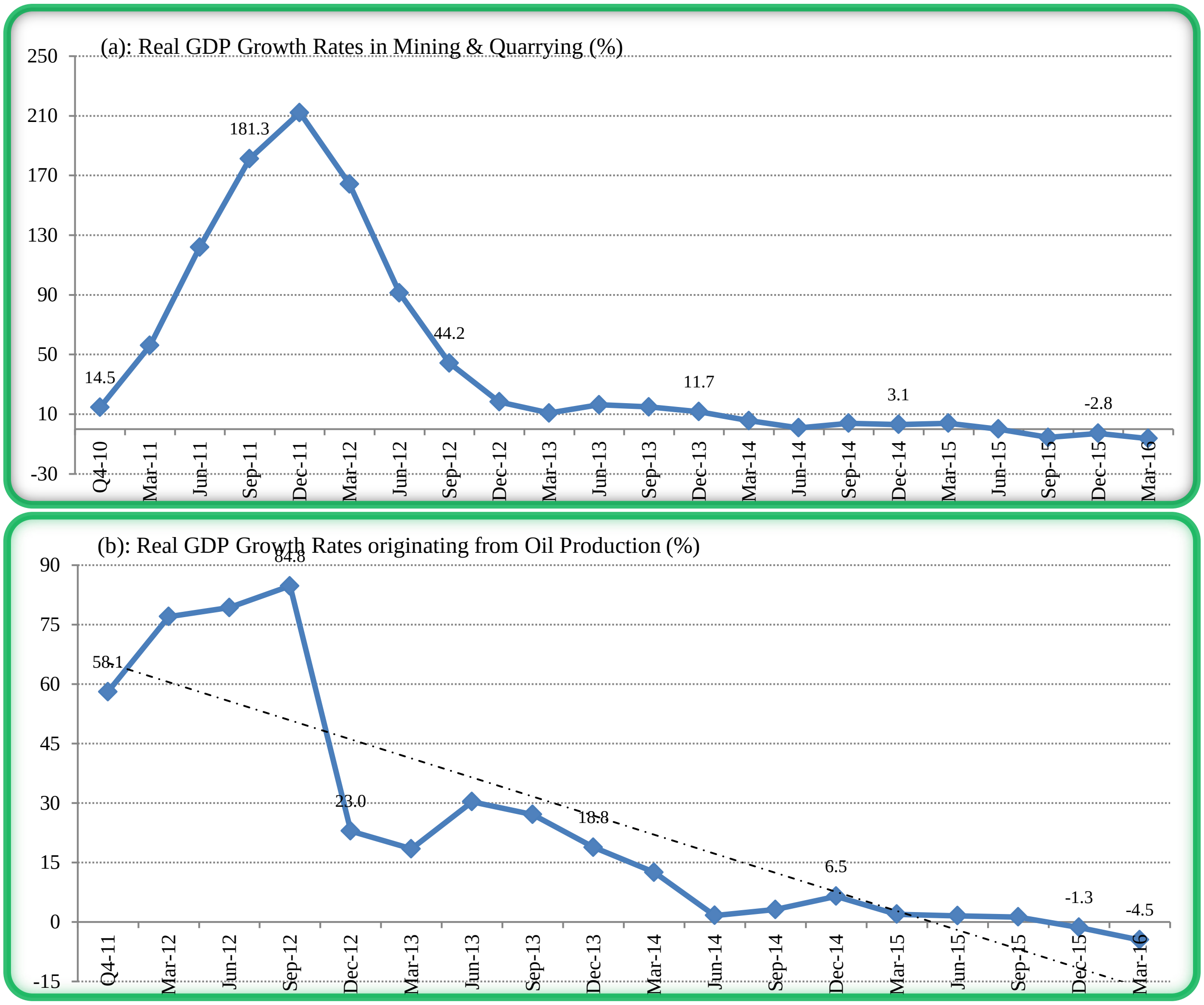
Data sources: Based on quarterly data series from the Ghana Statistical Service

Growth performance in the Agricultural sector, which is dominated by crops and cocoa production, has shown a rapid deceleration until about December 2012 when there was a sharp reversal, with GDP growth in the sector accelerating sharply to reach a peak of 21.7% in June 2013 [see Panel (b) of Chart 5].

The trend reversal has largely been attributed to record 'purchases' of cocoa beans in 2010/11 in which Ghana reportedly gained some 205 thousand metric tons from 'smuggling' from La Cote d'Ivoire in the midst of the political upheaval in that country — the so-called 'Gbagbo effect' referred to earlier.

Agricultural growth rates had since been falling steadily, plummeting into negative territory by mid-2014. The declining trend path reflects some worrisome trends in the cocoa industry as a whole, including loss of market share of Ghanaian premium cocoa, producer price setting and its associated net smuggling effect in neighbouring West African producing countries. Growth rates soared in June 2015 but have since slowed to an estimated 2.4% at the end of 2015

Chart 6: Seasonally-Adjusted Real GDP Growth Rates in M&Q and Oil Production (%)



Data sources: Based on quarterly data series from Ghana Statistical Service

Growth in the M&Q sub-sector, which is dominated by the extractive industries in gold mining and oil production, has been the main driver of growth trends in the Industrial sector, at least, since the entry into the Jubilee oil era. Growth performance in the sub-sector has largely been driven by the new oil and gas sub-sector. With the onset of oil production in commercial quantities in 2011, the sub-sector's growth rate shot up to an all-time high of 212% for that year. Thereafter, real GDP growth rate of the sector decelerated as sharply as it had accelerated, falling rapidly to 10.7% by end-2012.

The deceleration in growth slowed somewhat in the three years thereafter, with the seasonally-adjusted annual real GDP growth of the sub-sector declining to -2.8% at the end of 2015 [see Panel (a) of Chart 6].

Panel (b) of Chart 6 traces the growth path of real GDP since the onset of oil production in commercial quantities in 2011. It shows that the pace of real GDP growth originating from the oil production accelerated sharply from 58% at the end of 2011 to an all-time high of 85% in September 2012 but had since decelerated consistently reaching negative territory in December 2015 and the first quarter of 2016.

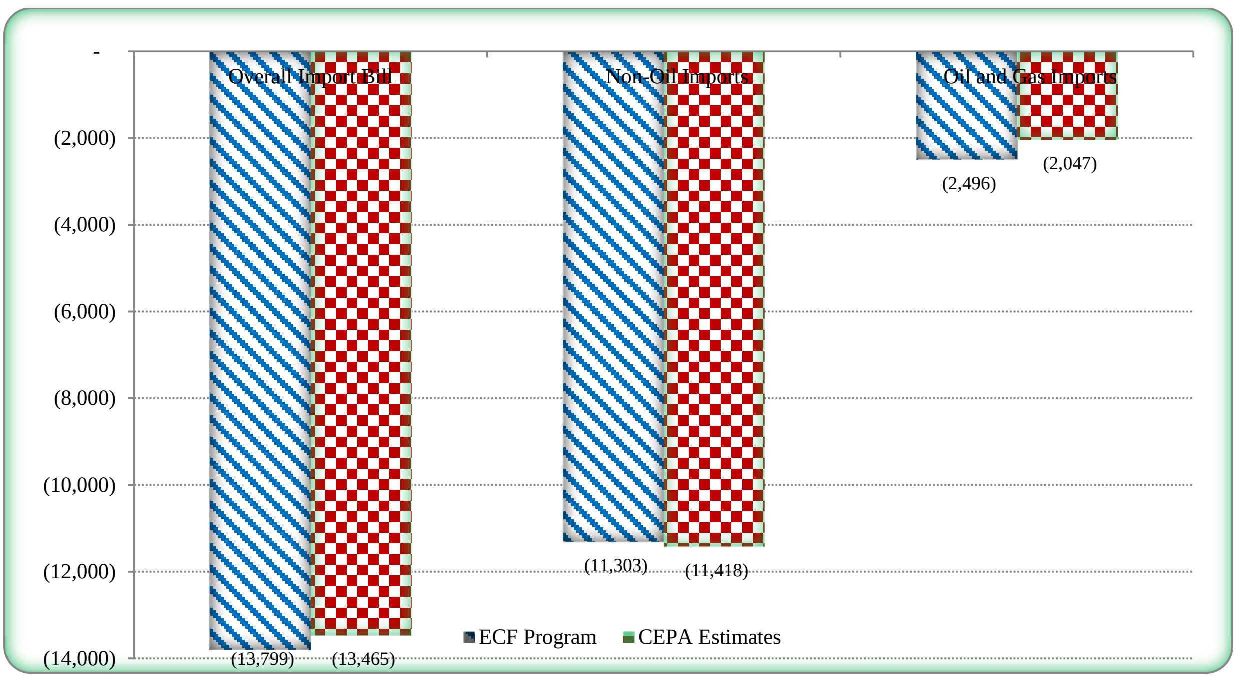
The sharp deceleration in the seasonally-adjusted growth rate of the sub-sector since September 2012 has been attributed to a number of factors, including:

- technical correction normally witnessed in extractive industries;
- production shortfalls vis-à-vis the expected target of 120,000 bbl per day; and
- persistent power shortages, especially in 2013 through 2014.

2.1.2 Merchandise Imports

On the demand side of the merchandise trade accounts, CEPA estimates an overall Import Bill that is slightly lower than that in the ECF-supported Program. The expectation is for Non-Oil Imports to increase to almost US$11.4 billion in 2015 compared to the Program target of US$11.3 billion. This implies a difference of some US$115 million on account of the non-oil bill. We anticipate, however, that this would be offset somewhat by some improvement of US$449 million in respect of petroleum products and gas imports on the assumption that more 'reliable' supplies of gas from the revamped Atuabo Gas Plant (Ghana Gas Company).

Chart 7: Merchandise Imports (US$ million)

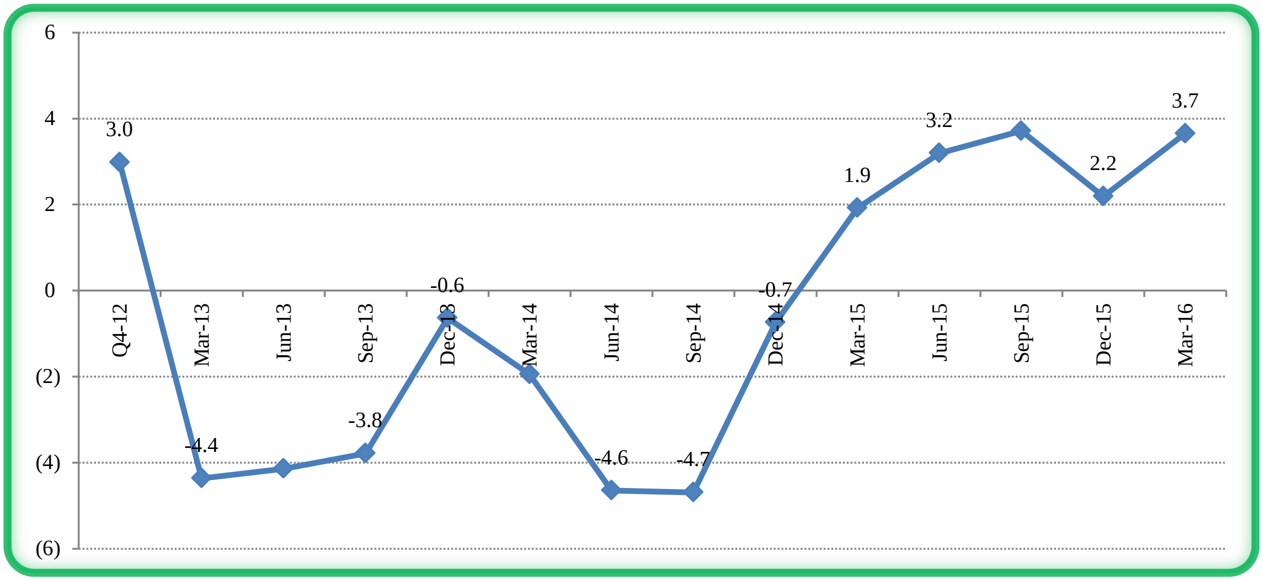


Regrettably, the Ghana Gas Company appears to be entrapped with some financing difficulties that could jeopardize its smooth operations. The Volta River Authority (VRA) is said to be massively indebted to the Company, making it impossible to service a Chinese loan. In present circumstances, it is critical that the Ghana Gas Company be made viable.

Demand-side Implications for Economic Growth in the Manufacturing sub-sector of Industry
The most disturbing of the developments in the Industrial sector has been the persistent deceleration of growth in the manufacturing sub-sector.

Real GDP growth rate in the sub-sector plummeted from 3% in 2012 into negative territory in both 2013 and 2014. This was on account of a combination of sharp real exchange rate depreciation, labour productivity losses resulting from wrangling over election results at the Supreme Court for over 8 months of 2013, and sporadic power outages popularly termed 'dumsor'.

Chart 8: Growth Implications for the Manufacturing sub-sector of Industry (%)



Some recovery was registered in 2015 as the exchange rate swung from real depreciation to real appreciation. The seasonally-adjusted growth rate trended upwards, reaching an estimated 2.2% by the end of the year.

2.2 The Current Account Deficit and its Financing

Typically, the current account of the balance of payments is composed of three items:

i. the merchandise trade balance account;
ii. the net services and investment income accounts; and
iii. transfer payments (official program grants and private unrequited transfers).

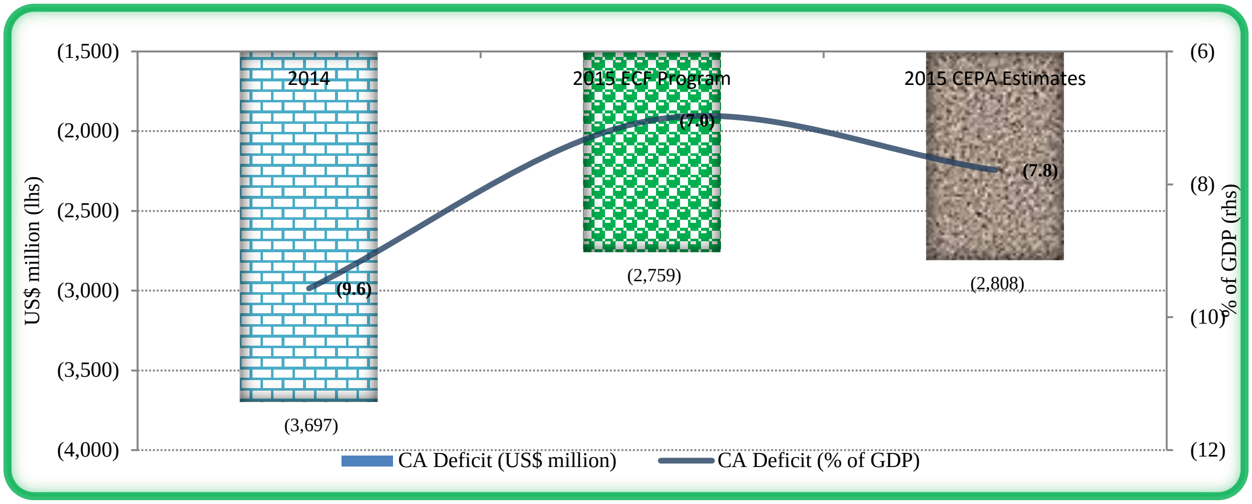
Text Table 1: Current Account Deficit and its Financing (US$ million)

	2014 Estimate	ECF Program, 2015	CEPA Estimates 2015	Difference CEPA-Prog
Merchandise Trade Deficit	(1,387)	(2,788)	(3,109)	(321)
Net Services, Income & Transfers	(2,310)	29	300	271
Current Account Deficit (incl official transfers)	(3,697)	(2,759)	(2,809)	(50)

CEPA estimates a larger surplus of US$300 million in respect of Net Services, Income and Transfers payments — some US$271 million more than anticipated in the Program [Text Table 1].

Combining these estimates with the CEPA projected merchandise trade deficit of US$3,109 million, yielded a current account deficit of US$2,809 million, which is some US$50 million more than anticipated in the Program. This is because of marginal estimated outflows from the services and investment income accounts and much improved private inward transfers relative to the Program targets [see Chart 9 and Text Table 1].

Chart 9: Current Account Deficit (US$ million & % of GDP)



Data sources: IMF Country Report No. 16/16, January 2016 and CEPA staff estimates for end-2015

In terms of GDP the CEPA estimate of the current account deficit at 7.8 percent is 0.8 percentage points higher than anticipated in the Program for 2015. Fortunately, increased flows of US$1 billion raised via a World Bank Policy-based Guarantee (PBG) could enable the GoG to redeem its existing debt stock and/or finance the relatively higher current account deficit [see Text Table 2].

Text Table 2: Financing the Current Account Deficit (US$ million)

	2014 Estimate	ECF Program, 2015	CEPA Estimates 2015	Difference CEPA-Prog
Current Account Deficit (incl official transfers)	(3,697)	(2,759)	(2,809)	(50)
Financing	3,660	2,476	2,976	500
Net Capital (Project Grants) Inflows	-	299	299	-
Financial Inflows (net)	3,660	2,177	2,677	500
Foreign Direct Investment (FDI)	3,357	2,941	2,941	-
Portfolio Investments (net)	836	500	1,000	500
Official Med & Long-Term Capital (net)	932	301	301	-
Private Med & Long-Term Capital (net)	(1,081)	(809)	(809)	-
Short-Term (net) - incl SWAPs to DMBs	(155)	(756)	(756)	-
Errors and Omissions (net)	(229)	-	(272)	(272)
Overall Balance of Payments	(37)	(283)	(129)	177

Data sources: IMF Country Report No. 16/16, January 2016; and CEPA staff estimates

Nonetheless, there may be potential difficulties not only in achieving the 'sustainable' current account deficit target in the medium term, there are also lingering reservations regarding continued reliance on expensive Eurobonds.

For example,

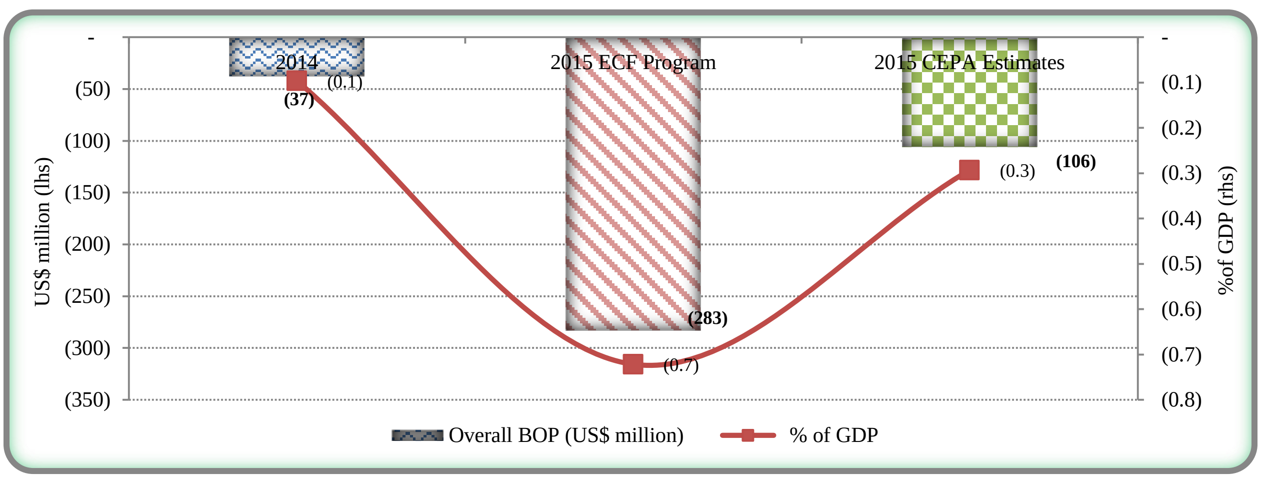
i. inflows from program and project grants are expected to gradually decline and taper off over the medium to long-term;
ii. consistent with Ghana's status as a lower-middle income country — implying limited access to concessional resources — external borrowing is expected to become increasingly non-concessional; and
iii. even though a series of issuances of Eurobonds are envisaged to rollover maturing Eurobonds, these would be repaid in amortization payments rather than as bullet payments similar to the 2014 Eurobond.

These realizations should be challenges that the monetary and fiscal authorities, working together, would have to grapple with going forward. In CEPA's view, all of this calls for continuous and sustained cooperation and collaboration between the Fiscal Authority (Ministry of Finance) and the Monetary Authority (Bank of Ghana). Fiscal intransigence and/or a "go-it-alone" approach may prove counterproductive and abhorrent, as it could intensify the pain of austerity and provoke social disturbances and unrest in the economy as a whole.

2.3 Overall Balance of Payments Deficit Improves over Program Target

Our third major finding is that the deficit on the overall BOP of US$283 million could improve to US$106 million, leading to a lower financing gap than envisaged in the Program.

Chart 10: Overall Balance of Payments (US$ million; and % of GDP)



Data sources: Based on data from IMF Country Report No. 16/16, January 2016 and CEPA staff projections

The relatively much improved overall BOP is on account of the US$1 billion (against a programed US$500 million) raised via a fifteen-year Eurobond issuance in late-September 2015, and notwithstanding the exceptional finance of some US$232 million from development partners as balance of payment support [see Text Tables 2 and 3].

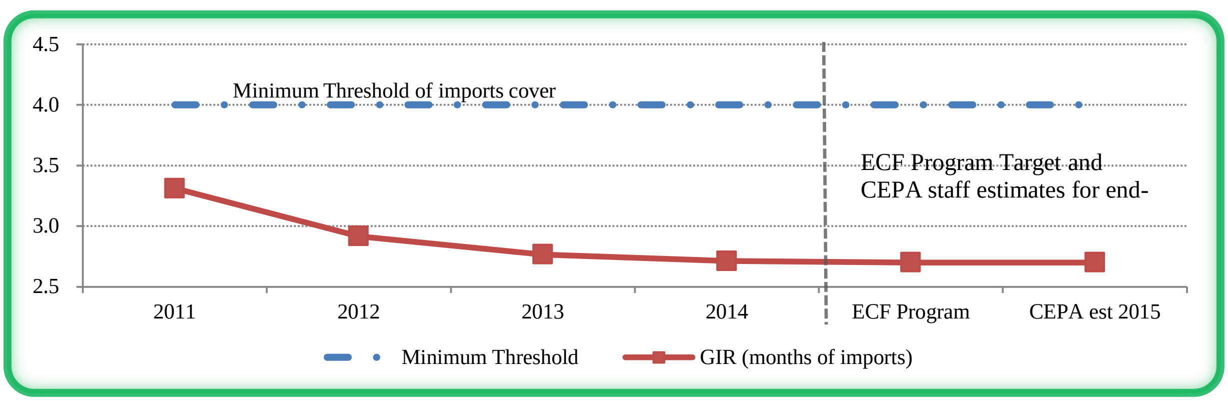
Text Table 3: Financing the Overall Balance of Payments Deficit (US$ million)

	Actual Outturn 2014	ECF Program 2015	CEPA Estimates 2015	Difference CEPA-Program
Overall Balance of Payments (BOP)	**(37.3)**	(283.)	(105.8)	177
Financing	37.0	283	105.8	(176)
Exceptional Financing	-	232	230	(2)
Multilaterals	-	200	200	-
Other Program Support	-	32	30	(2)
Δ Net International Reserves (- = increase)	49.0	51	(124)	(174)
Δ Gross International Reserves	238.0	(385)	(54)	331
Other NFA Reserves-Related Changes	(189.0)	139	(267)	(505)
Use of Fund Credit (net)	(12.0)	297	297	-
IMF Gross credit	-	359	359	-
Repayment of IMF credit and loans	(12.0)	(62)	(62	-
Memorandum Items				
Gross International Reserves (US$ million)	4,349.0	4,734.0	4,403	(331)
equivalent months of imports (G&NFS)	2.7	2.7	2.7	(0)
Net International Reserves (US$ million)	3,200.3	3,151	3,094	(57)
equivalent months of imports (G&NFS)	2.2	2.1	1.9	(0.2)

Data sources: Based on data from IMF Country Report No. 16/16, January 2016 and CEPA staff projections

It is to be understood that in addition to exceptional financing from development partners, the overall BOP deficit in the Program is to be financed through a draw-down of the net reserves (NIR) by US$51 million (including net use of IMF credit facilities involving gross credit of some US$397 million and repayment of US$62 million). The expectation of CEPA is for an accumulation of the net reserves stock by some US$124 million for the improved overall BOP to be adequately financed.

Chart 11: Stock of Gross International Reserves (months of imports of goods and services)



Data sources: IMF Country Report No. 16/16, January 2016 and CEPA staff estimates

External sustainability analysis undertaken by staff of the IMF suggests that rebuilding of the external gross reserves (GIR) position of the Bank of Ghana to at least four (4) months of imports cover should be *a key objective of the Program*. However, the records show that the stock levels of the GIR has remained below three (3) months of import cover, signaling that not only has Ghana failed to achieve the 4 months imports cover but also that the situation has been deteriorating year after year [see Chart 11].

The point to stress is that with very thin external buffers, the Bank of Ghana has very little wriggle room to intervene in the foreign exchange market, even if to "smoothen volatilities" in the market. Thin external buffers could also compromise the effectiveness of the inflation targeting (IT) regime of monetary policy under the Program.

It is CEPA's view that the GIR target of 3.1 months import cover set for 2015 in the Program could prove difficult to achieve, given the strong pressure on the Bank of Ghana to focus attention on its inflation target.

The program design captured the initial conditions in which Ghana was faced with external vulnerabilities — unsustainable external balances (the latest DSA had concluded that Ghana is at high risk of external debt distress) — as well as domestic imbalances (an inflation rate in double digits against the medium term target of 8 ± 2 percent). The macroeconomic framework therefore envisaged adjustments to both monetary and fiscal policies to **jointly address the external and internal imbalances on a simultaneous basis.**

The framework thus revealed the conflict in policy goals:

- loose money will help to depreciate the real exchange rate (RER) and will hence help close the external gap through the expenditure switching channel but inflation will rise even further — implying that monetary loosening must be combined with fiscal tightening;
- tighter money to achieve the inflation target would further appreciate the RER, elevate the external gap and deplete international reserves and/or increase external debt. Once more, both monetary and fiscal adjustments must play a role.

The results thus far pose the following problem: nominal GDP appears to be rising faster than projected. Both real GDP and its implicit deflator are growing faster than projected. Either the fiscal consolidation is in reality weaker than suggested by the official data or the fiscal multiplier was over-estimated by a wide margin. In other words, we are confronted with fiscal intransigence — the fiscal authority is unwilling or in any case unable to play its role and de facto the BoG is operating on a 'go-it-alone' basis.

3.0 OUTCOMES OF PROGRAM REVIEWS BY THE FUND

Since its approval by the Executive Board of the IMF, the ECF-supported Program has been reviewed three times — the first in July 2015, the second in January 2016, and the third in May 2016.

With specific reference to external trade and payments, the reviews — which respectively focused on April 2015, August 2015, and December 2015 data — involved monitoring three performance criteria (PC) under the arrangement:

- a floor on the net international reserves of the Bank of Ghana — to support efforts at maintaining adequate external buffers against a variety of exogenous shocks, including sharp swings in the terms-of trade, and volatile financial flows;
- a continuous non-accumulation of new external arrears; and

- a ceiling on contracting or guaranteeing of new external non-concessional debt.

The outcomes of the first two reviews revealed that whereas the performance criterion on the NIR was satisfactorily met, those on the continuous non-accumulation of external arrears and contracting or guaranteeing new external non-concessional debt were missed

Yet, in August 2015 the IMF staff reportedly 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 reportedly 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 end-August.

Again, in the assessment under the second review, the IMF reported that:

> …… the continuous PC on non-accumulation of external arrears was missed <u>due to some minor payment delays stemming from discrepancies in the debt database projections and uncertainties about some debt obligations</u> [see Statement by Mr. Mojarrad, Executive Director for Ghana; IMF Country Report No. 16/16, January 13, 2016; emphasis added].

In completing the review, the Executive Board also granted a waiver for the non-observance of the performance criterion regarding non-accumulation of external arrears. Thus, in the latest Country Report of January 2016, it is observed that:

> The <u>non-concessional debt limits</u> were increased from US$1 billion to US$2.5 billion (in the context of the first review) <u>to accommodate the originally-planned Eurobond issuance of up to US$1.5 billion, some projects integral to the development program for which concessional financing is not available, and a World Bank loan</u>. In addition, an indicative ceiling of US$100 million on concessional loans was created to address vulnerabilities associated with external debt. ….. Up to end-August, zero non-concessional external loans for projects and concessional external loans of US$200 million had been contracted. The World Bank has released US$150 million loan in August [MEFP, paragraph 82, pp. 57-58; emphasis added].

For reasons bordering on delayed finalization of some documentation by the Ghanaian authorities, the third review was silent on all three PCs on trade and payments even though targets had been set for them. At CEPA, we have been constrained by data accessibility in our efforts at monitoring the PC criterion on non-accumulation of external arrears and are therefore unable to make any concrete pronouncement until the detailed data is made available to us.

Regarding the PC on the net international reserves (NIR), CEPA is well aware that for program monitoring purposes, net international reserves are defined as short-term foreign assets of the BoG minus short-term external liabilities contracted by the central bank for reserve management purposes. These BoG liabilities do not include swaps contracted with resident banks and fully collateralized credit lines with foreign institutions. The definition differs from the one reported in the Balance of Payments and Monetary Survey which reflect a more traditional definition of foreign assets and liabilities based on residency basis.

The problem we have been facing at CEPA is how to take out the relevant short-term liabilities — the foreign currency deposits at the BoG held by resident deposit money banks (which includes the stock of swaps deals with resident banks payable in foreign exchange) — until these are promptly published by the

Bank of Ghana. It is also not very clear to us whether the short-term liabilities in respect of BoG's obligations to the IMF should also be netted out.

4.0 OUTLOOK AND CONCLUSIONS

The outlook remains challenging and risks are skewed to the downside, both in terms of achieving sustainable levels of trade and current account deficits and securing adequate external buffers primarily to cushion exogenous shocks to the economy while meeting the country's financing needs.

In the short- to medium-term, a narrowing of the current account deficit would depend critically on a significant swing to favorable terms of trade and how quickly the cocoa harvest and gold production recover. Current developments are signaling that while global markets for cocoa may continue to experience relatively stable prices with slight declines in the coming year, the projected 2015/16 cocoa crop and export volumes for Ghana could fall. Moreover, a further decline in gold prices could also lead to output cuts and labor layoffs that may consequently impact on export earnings. Typically, price declines in extractive industries call for cost adjustments that could lead to either labor layoffs or output cutbacks or both.

Together with very little changes in the overall import bill, these may most likely result in a widening (not a narrowing) of the trade deficit with adverse consequences for the current accounts. A further increase in the current account deficit would reduce an already low reserve buffer, triggering increased exchange rate pressures on the domestic currency to depreciate.

Secondly, external financing of the current account deficit is likely to become scanty and more expensive as access to financing becomes increasingly tight. Meanwhile, external non-concessional foreign currency borrowing is expected to continue to play a role in reducing pressures in the domestic debt market and stabilize exchange rates.

As has been suggested by the Fund staff, in order to ensure that such borrowing strengthens confidence in the program:

i. it must be carefully designed to avoid jeopardizing debt sustainability;
ii. it must be anchored in a comprehensive analysis of cost-risk tradeoffs of alternative debt management strategies, especially of risks to debt dynamics associated with exchange rate fluctuations;
iii. it must be aligned with well-established principles of debt management, such as the need to avoid locking into high interest rates for very long maturities;
iv. a reduction of risk premia over the medium term should be an important objective; and
v. it is not undertaken at a cost that is unduly high relative to that of similar debt issued by peer frontier issuers.

Conclusion

Financing gaps in the domestic bond market (i.e., under-subscriptions — bonds tendered falling below target}; in the Eurobond market (markets closed to Ghana) and the 'musical chairs' at BoG in the context of delayed passage into law of the BoG Act for the elimination of fiscal dominance of monetary policy make resort to seigniorage (money printing) increasingly likely.