

THE IMF BAILOUT: WILL THE ANCHOR HOLD?

DISTINGUISHED SPEAKER SERIES LECTURE

by:

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Ladies and Gentlemen

I would also like to thank all of you here present for undertaking the journey to this beautiful Miotso campus of Central University College. Almost exactly a year ago, on March 25th 2014, I had the privilege and honour of delivering a lecture on “Restoring the Value of the Cedi”. This was at the height of the crisis of the depreciation of the cedi. During that lecture, I noted that given the state of the economy, Ghana would likely end up requesting an IMF

bailout if appropriate action was not taken. Today, the IMF bailout has become a reality. It is only appropriate that this second lecture critically examines this IMF bailout program, its implications and whether it would provide the anchor for growth and prosperity in Ghana.

GHANA'S ROAD TO THE 2015 IMF BAILOUT

Mr. Chairman, for our benefit and for a little history, let me state that the International Monetary Fund (IMF) was founded in 1945 with a responsibility to maintain the stability of the international monetary system (i.e. the system of exchange rates and international payments that enable transactions between countries). Ghana is one of 188 members of the IMF. Each member of the IMF has a quota that it contributes to the Fund. The quota is set in relation to a country's importance in the international financial system. It is primarily from these quota contributions of member countries that the IMF lends to countries in distress (usually facing balance of payments problems). IMF financing provides countries with the breathing room to resolve the underlying problems. Even though technically classified as "balance of payments support", it provides support to the budget by making possible expenditures such as debt service and essential imports.

When a country makes a request for IMF financial assistance, the IMF designs a program in collaboration with the country's authorities to deal with the ailment diagnosed as causing the underlying balance of payments difficulties. Continued IMF financing under these circumstances, is conditional on the effective implementation of the designed program. In doing so, the IMF takes measures to safeguard the resources of its member countries that are being lent. The IMF is not a charity.

Ghana is no stranger to IMF bailouts. Ghana has had several programs with the IMF between 1967 and 2012 (These include programs in 1967, 1972, 1983, 1999, 2001, and 2009). The most recent IMF program with Ghana was between 2009 and 2012.

Ghana's most recent request for an IMF bailout has taken domestic and international observers as well as analysts by surprise. This is because Ghana was the star of the Africa rising story, the toast of the international development community, and the benchmark for other African countries for a number of reasons, including the following;

- Ghana's GDP more than quadrupled between 2001 and 2008, moving it from a HIPC country to a lower middle income country.

- Ghana received HIPC relief of \$4.2 billion dollars after HIPC completion in 2004
- Ghana discovered oil and gas in commercial quantities in 2007 and started exporting oil in 2010
- By 2011 Ghana was one of the fastest growing countries in the world with GDP growth estimated at 15% and government touted “unprecedented achievements” in growth and macroeconomic stability.

Notwithstanding these achievements, four years after oil production began, Ghana has found itself in need of a bailout from the IMF. The question is Why? How did it happen?

THE DISCOVERY OF OIL, ELECTIONS AND PUBLIC FINANCES

With the discovery of oil in 2007 the government of Ghana was determined to make sure that Ghana’s oil resources were managed in a manner to avoid the dreaded oil curse. In this regard, government brought together the various stakeholders to chart the way forward and to learn from the experiences of countries such as Nigeria and Norway in terms of best

practices and also what to avoid. The majority of the Ghanaian people were clear in their minds that Ghana should not end up with the issues that had bogged many African oil producing nations, most notably Nigeria. To underpin good governance in the oil sector, these stakeholder discussions and public consultations resulted in the passage of Ghana's Petroleum Revenue Management Act (PRMA) and the Petroleum Commission Act in 2011 based on best practice across oil producing countries.

Deteriorating Public Finances

Notwithstanding all the effort to avoid the oil curse, public finances began to deteriorate as the 2012 presidential and parliamentary elections drew closer. In the 2012 election year, Ghana's budget deficit was a whopping GH¢8.7 billion, amounting to 12.0% of GDP. This is the highest recorded budget deficit in Ghana's history. The crux of the problem was that government spending in 2012 increased astronomically to 31.0% of GDP even though government revenues amounted to 18.6% of GDP for the year. This came on the back of a promise by the government to ensure that it maintained fiscal discipline and that previous over-expenditures that had characterized

many of our election years were not repeated. On the contrary, the government abandoned all fiscal discipline so as to win the 2012 elections. Following the 2012 election, the government continued to maintain an expansionary fiscal stance and this led to a further deterioration of public finances.

The deterioration of public finances has resulted in government being cash strapped and unable to meet its obligations on statutory payments (for health education and local government) as well as non-statutory payments:

- The District Assembly Common Fund (DACF) is in arrears
- The Ghana Education Trust Fund is in arrears
- The National Health Insurance Scheme is in arrears
- School Feeding program is in arrears
- Payments to government contractors are in arrears

Recently, the Ghana Medical Association (GMA) warned that Ghana is inching towards a return to the dreaded cash-and-carry-system in the delivery of health services because hospitals across the country have run into complete bankruptcy due to failure by the National Health Insurance

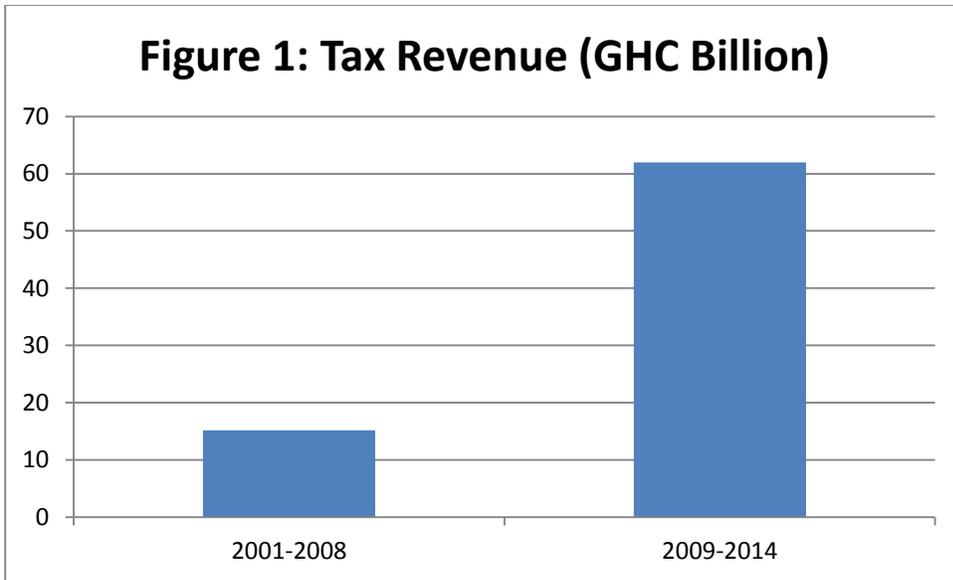
Authority (NHIA) to pay claims made by service providers¹. Furthermore, the cholera outbreak that occurred last year was linked to the local authorities being unable to pay for sanitation services.

Mr. Chairman, what is surprising about the current state of public finances is that over the last six years, this government has had available to it more financial resources than any government in the history of Ghana and so unlike previously, the current predicament cannot be blamed on a shortfall in resource inflows.

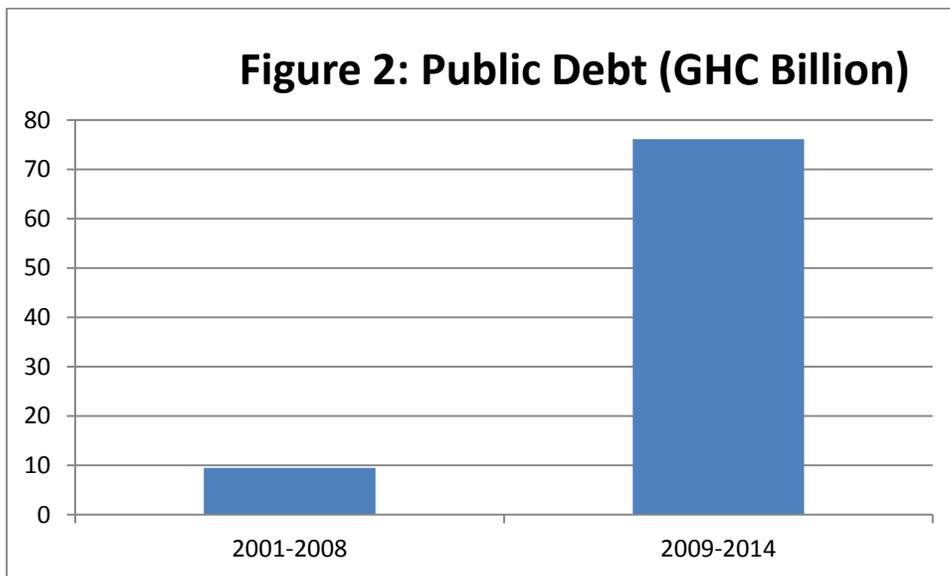
The financial resources that have been available to this government are actually mind boggling.

- In the eight years between 2001 and 2008, the total tax revenue collected was GHC 15.2 billion. In contrast, the government has collected a total of GHC 62 billion in the last six years (2009-2014) in taxes. (Figure 1).

¹ <http://www.myjoyonline.com/news/2015/March-3rd/we-are-back-to-cash-and-carry-gma-executive-warns.php#sthash.QKVdoeOe.dpuf>



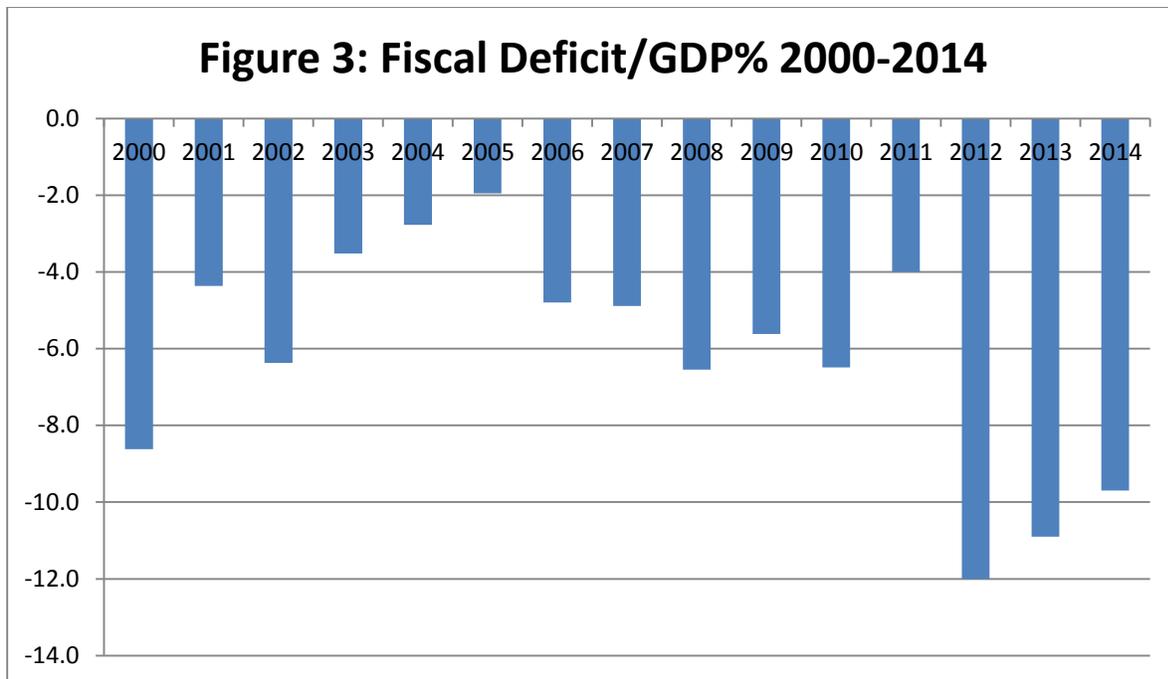
- In the last six years, Ghana's total debt has increased from GHC9.5 billion in 2008 to GHC76.1 billion at the end of 2014 (Figure 2).



- Ghana's gold exports between 2001 and 2008 amounted to \$9.0 billion dollars. Between 2009 and 2014, total gold exports have amounted to \$25 billion dollars. Government has therefore earned significantly more from the revenues associated with these exports in the last six years.
- Ghana's cocoa exports between 2001 and 2008 amounted to \$7.4 billion dollars. Between 2009 and 2014, total cocoa exports have amounted to \$14.5 billion dollars. Government has similarly earned significantly more from the revenues associated with these exports in the last six years.
- Indeed, cocoa and gold prices were 50% higher in the period 2009-2014 than the 2001-2008 period.
- Ghana has also become an oil exporter during the period of the NDC government. Ghana has exported \$13.7 billion of oil in the last four years and has earned some \$3 billion from oil during this period. There were no oil revenues accruing from oil exports during the 2001-2008 period or for that matter in any period of Ghana's history.

The question therefore is if this government has had available all these resources in terms of tax revenue, loans, and revenues from gold, cocoa and oil exports amongst others, then why is it that public finances are in such a bad state to the extent that we need an IMF bailout?

Mr. Chairman, this situation with regards to Ghana's public finances has arisen because of a major increase in government expenditures relative to revenues between 2011 and 2014. While government tax revenue averaged 18.9% of GDP between 2011 and 2014, government expenditures increased of GDP from 20.1% of GDP in 2011 to 31.0% of GDP in 2012 before declining to 28.2% of GDP at the end of 2014. It should be noted that the fiscal deficits as a percentage of GDP in the last three years (at 9.5%, 10.9% and 12%) have exceeded the 8.6% deficit in 2000 that sent the economy into a tailspin.



Mr. Chairman, another reason why Ghana is looking for an IMF bailout is corruption. The increased fiscal deficits have also been compounded by pervasive corruption in the public sector in the areas of over-invoicing of contracts underpinned by the practice of sole sourcing in the award of over-priced contracts, and corruption related to scandals such as judgment debts, SADA, SUBAH, GYEEDA, ghost names on government payroll, etc.

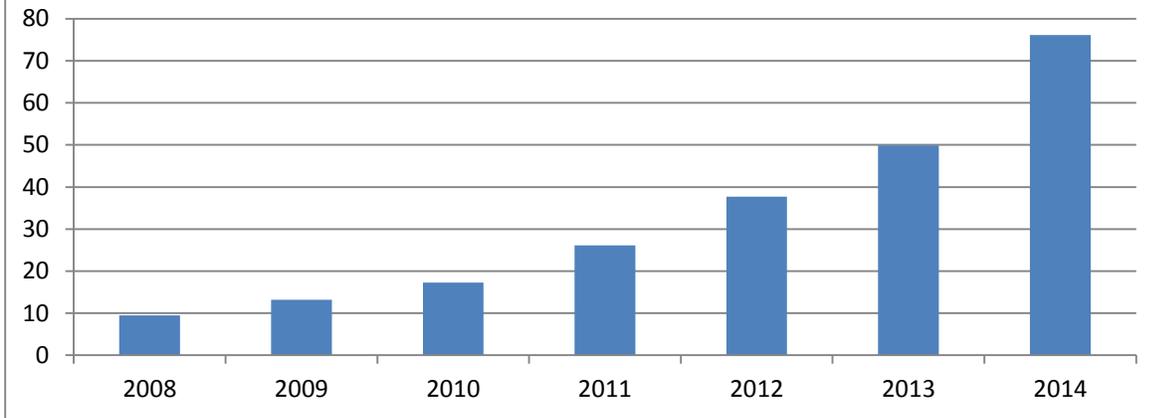
What we have in Ghana today is not just corruption but corruption with impunity. It is corruption by people who have no fear for the consequences because they know they can conspire to get away with it. These acts of

corruption are very costly to the nation and take away the opportunities for government expenditure in critical areas. Former President Rawlings has recently noted that the corruption for which he overthrew the government in 1979 is not up to 10% of the corruption we are seeing today.

Ballooning and Unsustainable Public Debt

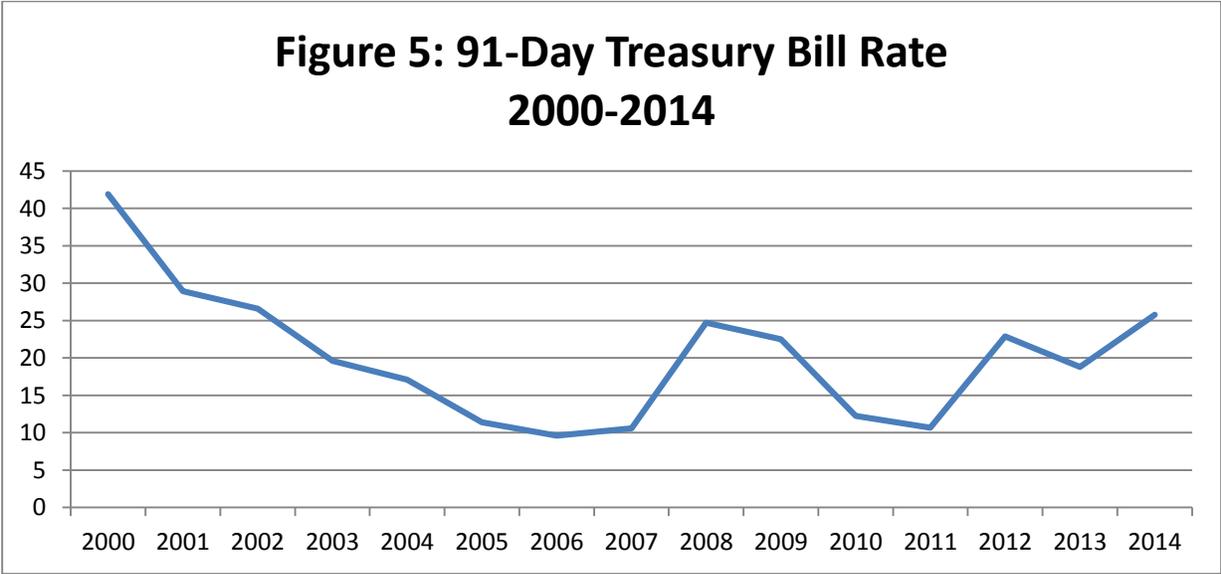
Mr. Chairman, probably the most significant contributor to Ghana's request for an IMF bailout is the ballooning and unsustainable public debt less than a decade after being granted HIPC debt relief to the tune of \$4.2 billion. The debt relief obtained under HIPC and the accompanying fiscal policy stance resulted in a significant reduction of the debt burden. By the end of 2008, Ghana's total public debt stood at GH¢9.5 billion (33% of GDP). In the last six years however, the stock of public debt has seen a dramatic increase to GH¢76.1 billion (67.1% of GDP) at the end of 2014 (Figure 4). This is an increase in the stock of debt by **700%** (GH¢66.6billion) over a six year period and it represents an average increase in the stock of debt by 116% a year.

**Figure 4: Ghana's Total Debt
2008-2014**



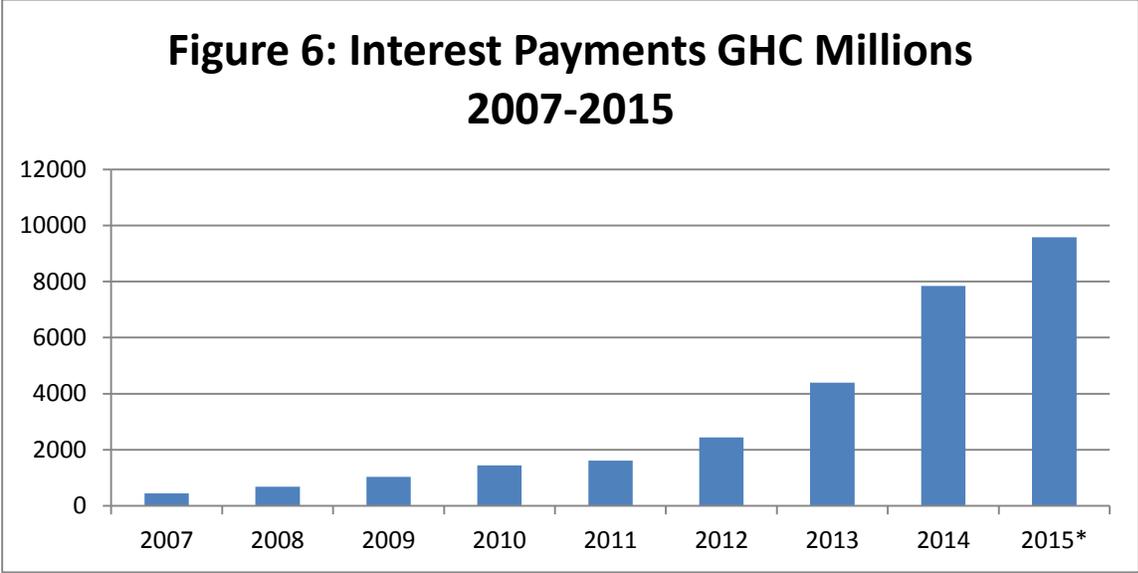
As I have said before, this is a frightening rate of accumulation of debt by any standard and demonstrates a degree of recklessness in the management of Ghana's debt. The Government is however on record as saying that it has actually been undertaking "smart borrowing". One can only shudder to think what "not so smart borrowing" would look like. The Minister of Finance has also recently stated that the increase in the debt stock "is not our fault". Really? Was it not this same government that responded to warnings about the rate of borrowing by saying it had the capacity to borrow and would continue borrowing? How then can it not be their fault? Who increased the debt stock by GHC66.6 billion in six years? Is it the fault of some dwarfs? Who did the "smart borrowing"?

With such large scale borrowing, government is crowding out the private sector which is unable to borrow to grow their business. Risk free Treasury bill rates are around 25% (up from 10.6% in 2011) and bank lending rates are on the rise because of excessive government borrowing. Lending rates are now 30 percent. Figure 5 shows that the 91-Day Treasury bill rate which was on a steady declining path between 2000-2007 but has subsequently been on a more volatile upward trend. In aggregate, the 91-day Treasury bill rate declined from 41.9% in 2000 to 24.8% in 2008 (a reduction of 17 percentage points). The rate further declined to 10.6% in 2011 but has since increased to 25.8% in December 2014 (an aggregate increase of one percentage point over the period 2008-2014).



Source: Bank of Ghana

Mr. Chairman, the interest burden of this high public debt stock has proven to be extremely high. In 2015, interest payments alone on the debt would amount to GHC9.57 billion. As Figure 6 shows, interest payments have increased from GHC 679 million in 2008 to a projected GHC9.57 billion in 2015 (an increase of 14 fold). Ghana’s total debt in 2008 was GHC9.5 billion but interest payments in 2015 alone would amount to GHC9.5 billion.



Interest payment as a percentage of GDP has also increased from 2.8% in 2008 to 7.1% in 2015 (Figure 6b).

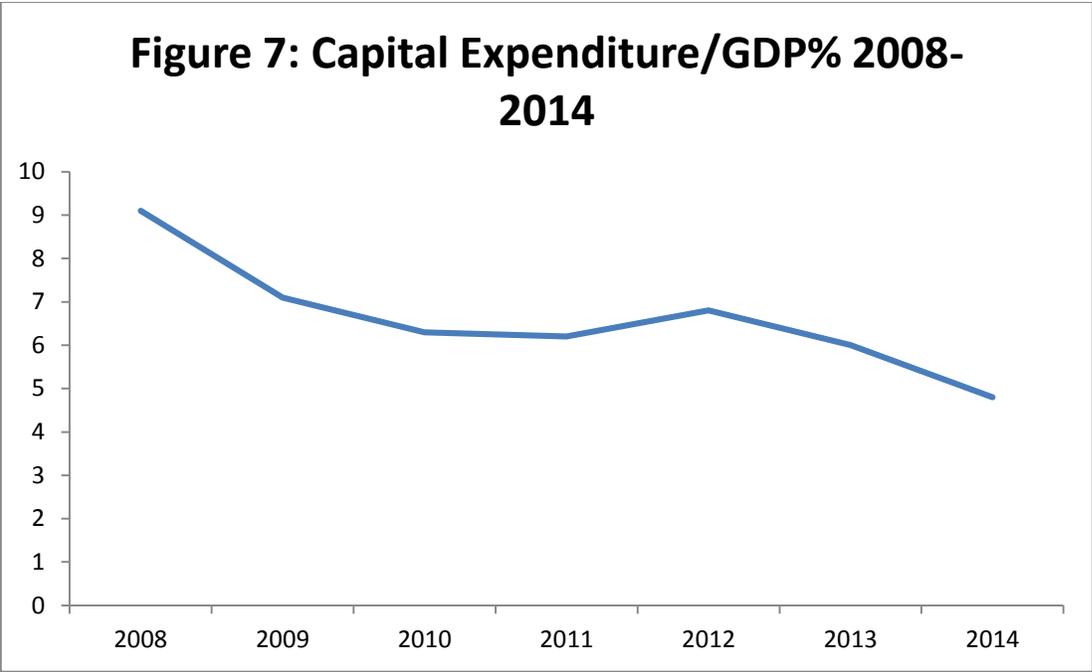
VRA and its ability to import crude oil for the generation of power. This situation has in turn forced VRA to over use the Akosombo dam by 30% more than recommended since 2012 thereby causing the drop in the level of the dam. Mr. Chairman, the untold story about the erratic gas supply from Nigeria is that Ghana owes Nigeria Gas US\$100 million. Nigeria Gas is therefore dragging its feet with regards to the supply of Gas while this amount is unpaid. Ultimately, the dumsor problem is more of a financial problem than a technical one.

Mr. Chairman, Ladies and Gentlemen, it would also interest you to know that Ghana has recently been sanctioned by the African Development Bank (AfDB) for non-payment of debt obligations due. This sanction means that signature of new AfDB loan agreements, disbursements on all AfDB on-going projects and the granting of any new loans have been suspended until the situation is rectified. The sanctions were effective in January 2015. In this regard, Ghana regrettably joins an exclusive list of nations currently under AfDB sanctions. The other countries are Somalia, Sudan, Zimbabwe, and Djibouti. Ghana's arrears on its AfDB debt obligations only serves to emphasize the pressure on government cash reserves as well as the poor debt management. You cannot treat external debt obligations in the same

way as you treat your obligations to the NHIS, DACF, GETFUND or Road Fund.

Mr. Chairman, at 67% of GDP, Ghana's debt stock has crossed the critical 60% of GDP level that developing countries with limited access to capital flows should worry about in terms of debt sustainability. In fact, Ghana is right back to the debt unsustainability that led to HIPC. However, HIPC debt relief will not be available again. Ghana's status can thus best be described as that of a Highly Indebted Lower Middle Income Country (HIMIC).

Mr. Chairman, notwithstanding the massive increase in the debt stock, capital expenditure as a percentage (%) of GDP has actually been on the decline from 9.1% of GDP in 2008 to 4.8% by 2014 (Figure 7). Capital expenditure as a percentage of GDP averaged 11% for 2001-2008 (without oil) while that for 2009-2014 has averaged 6% (with oil).



This means that contrary to all the government claims of an increase in infrastructure expenditure on projects all over the country, the reality is that Ghana's expenditure on infrastructure is declining. The numbers indicate that relative to GDP, this government is investing about half what the previous government invested in infrastructure. It is in fact a travesty that Ghana before the discovery of oil was spending a higher proportion of its income on infrastructure investment than after the discovery of oil and the massive increase in the debt stock. This decline in investment in infrastructure runs counter to what one would have expected. Even though the allocation of oil revenues is skewed towards infrastructure, the decline in

capital spending means that the infrastructure expenditure from oil revenues is substituting for rather than adding to existing capital expenditure. After all the loans, all the taxes and all the oil, how can investment in infrastructure relative to GDP be at half the level that it was in 2008 (without oil)? This means that if the government had just maintained the 2001-2008 levels, it would be doing twice as much as it is doing now in the areas of roads, water, schools, hospitals, energy, etc. The sad decline in infrastructure investment partly explains why GDP growth has declined significantly from 15% in 2011 to a projected 3.5% in 2015.

Mr. Chairman, it is therefore clear that most of the increase in the debt stock has not gone into capital expenditure. A case in point is the utilization of \$1 billion Eurobond proceeds received in 2014. While the Government sought to convince the public that the sovereign bond monies had been used for infrastructure investment, the evidence shows otherwise. A look at the Bank of Ghana Monetary Accounts for 2014 reveals the true picture, which is that the sovereign bond has rather been used to reduce Government indebtedness to the central bank and not applied for the purpose for which the funds were borrowed. This is why the government cannot seem to be able to answer the simple question as to what the funds were spent on. One

wonders why our economic managers can't just be honest when these issues come up?

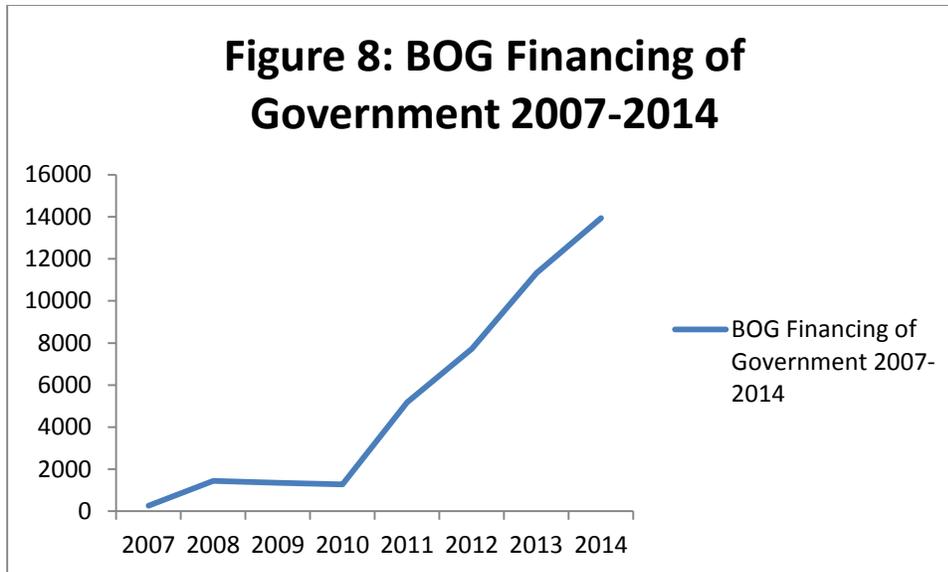
Mr. Chairman, I wonder how this high rate of borrowing and interest payments which has led to an increase in interest rates, deprived the state of resources in several critical sectors like health and education, led to lower investment in infrastructure and led the country to the doors of the IMF for a bailout, can be described as "smart". This must indeed be a new form of "smart" we are not aware of. It is like asking an alcoholic why he is drinking so much and he tells you that he is doing "smart drinking".

LOOSE MONETARY POLICY

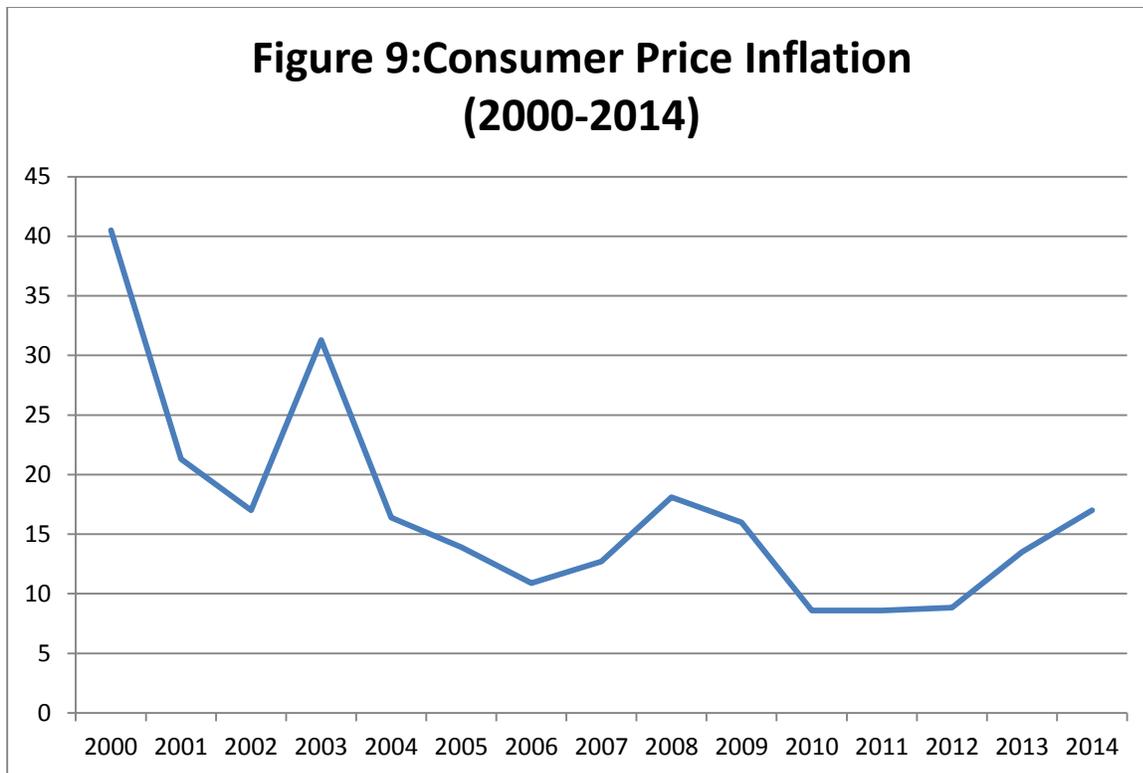
Mr. Chairman, I now turn to the role of the Bank of Ghana's monetary policy in our journey towards the IMF bailout. The Bank of Ghana is responsible for maintaining price and exchange rate stability in Ghana. To do this, the Bank of Ghana adopted an inflation targeting monetary policy framework in the context of a market determined exchange rate regime in 2002. The inflation targeting monetary policy framework uses the interest rate as the instrument

to maintain price stability. If inflationary expectations are heightened, the framework would generally call for an increase in interest rates and vice-versa. A disciplined adherence to this framework is important for success but the framework can easily be unraveled if the central bank increasingly becomes the source of financing government fiscal deficits over time. Unfortunately this has been the recent experience of Ghana.

Mr. Chairman, *as I stated last year*, excessive fiscal expansion creates problems in many developing countries because it tends to be largely monetized and the excess injection of liquidity results in inflation and exchange rate depreciation. This has been Ghana's experience in the last four years. There has been a dramatic increase in central bank financing of government recently (i.e. equivalent to the printing of money), in addition to borrowing to finance the fiscal deficit. Central bank financing (net claims on government) has increased from GH¢1.45 billion in 2008 to GH¢13.95 billion by 2014, an 863% increase (Figure 8).



Mr. Chairman the excess printing of money to finance the fiscal deficit causes inflation. In accommodating Government in this manner, the Bank of Ghana is by itself undermining the value of the currency that it is required by law to protect. After declining from 40.5% at the end of 2000 to 18.1% at the end of 2008 (an aggregate decline of 12.0 percentage points) inflation further declined to 8.5% in 2010 but has since increased to 17% by the end of 2014 (an aggregate decline of 1.1 percentage point between 2008 and 2014) - Figure 9. Non-Food inflation increased from 19.1% in 2008 to 23.9% by the end of 2014. I will return to these official inflation numbers later.



Source: Bank of Ghana

Furthermore, the inflation targeting framework that the Bank of Ghana is pursuing is inconsistent with a simultaneous attempt to control the exchange rate. In general you cannot maintain a fixed exchange rate and at the same time have an independent monetary policy. Unfortunately and very surprisingly, the Bank of Ghana tried to do this in 2014 in the face of a major depreciation of the cedi.

The Bank of Ghana imposed foreign exchange controls. In particular,

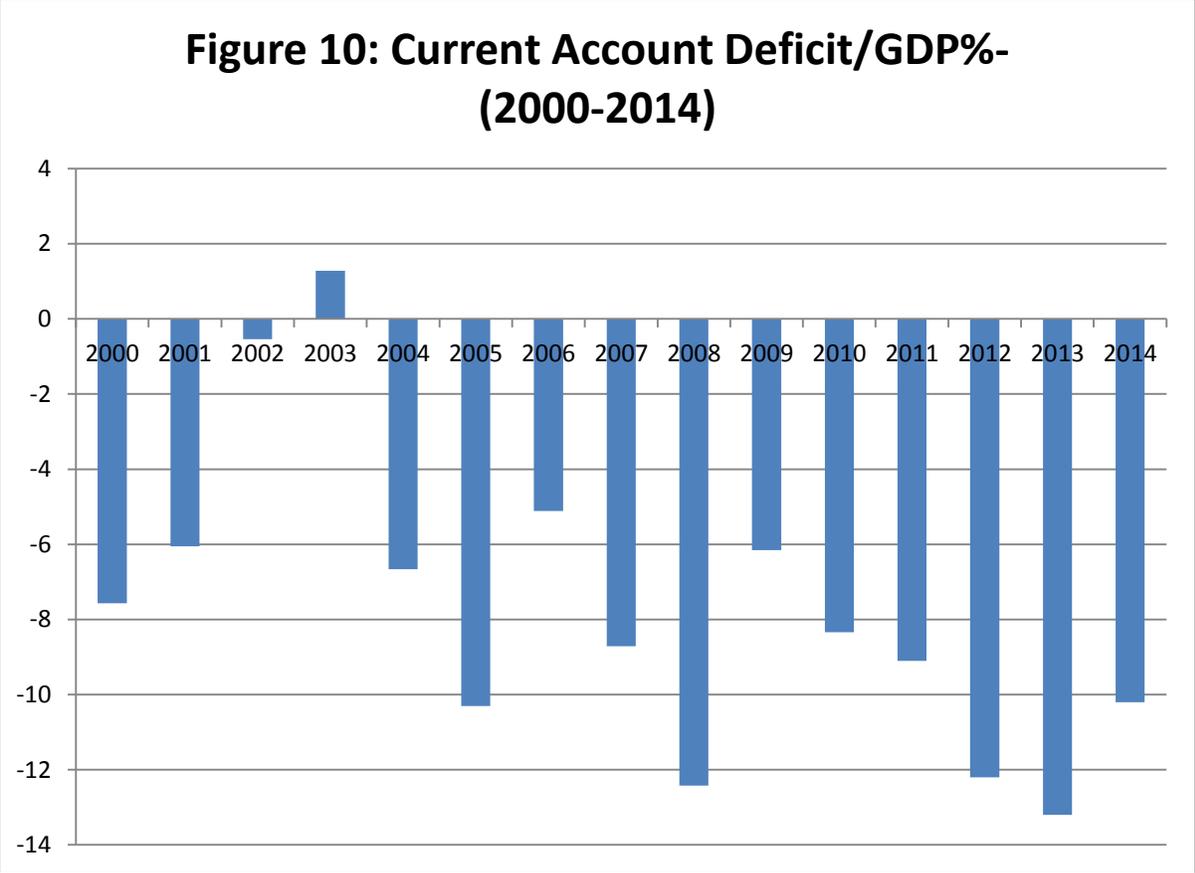
1. Exporters were directed to have their export proceeds repatriated within 60 days and such earnings should be converted into cedis within 5 days of receipt.
2. Withdrawals from foreign currency accounts (FEA and FCA) would be paid in cedis except for \$10000 for travel purposes.

Not surprisingly, these measures added an element of uncertainty to Ghana's exchange rate regime and created panic in the foreign exchange market.

These exchange controls resulted in a wide divergence between the Bank of Ghana rate and the interbank market and forex bureau exchange rates. The mismanagement of the exchange rate and the resulting depreciation proved to be very costly to the Ghanaian economy, affecting individuals and firms alike.

Deteriorating External Payments Position

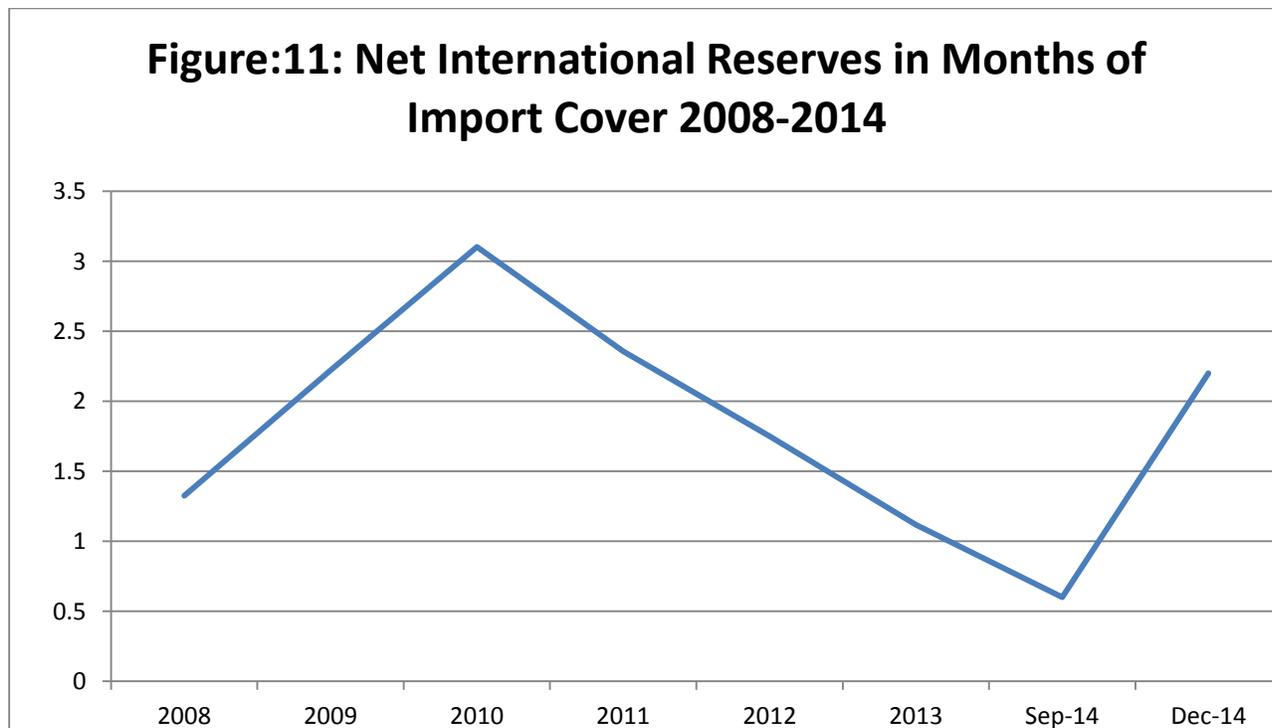
Mr. Chairman, another major factor that has led to Ghana seeking an IMF bailout is that Ghana’s external payments position has also deteriorated (consistent with the deterioration of public finances) with increasing current account deficits and a fragile foreign exchange reserves position. The current account of the balance of payments has seen a steady deterioration over the last four years, increasing from a deficit of \$2.77 billion (8.3 percent of GDP) in 2010 to \$4.92 billion (12.2 percent of GDP) in 2012 and \$5.8 billion (13.2 percent of GDP) in 2013. The deficit narrowed to \$3.6 billion (10.2% of GDP) in 2014 (Figure 10).



Source: Bank of Ghana

This is the first time in Ghana’s history that the current account has registered double digit deficits three years in a row.

The persistently high current account deficits contributed to a significant decline in Ghana’s foreign exchange reserves. Ghana’s net international reserves declined from a peak of \$4.4 billion in 2011 (equivalent to 3.1 months of import cover to \$950 million in September 2014 (equivalent to 0.6 months of import cover) – Figure 11.

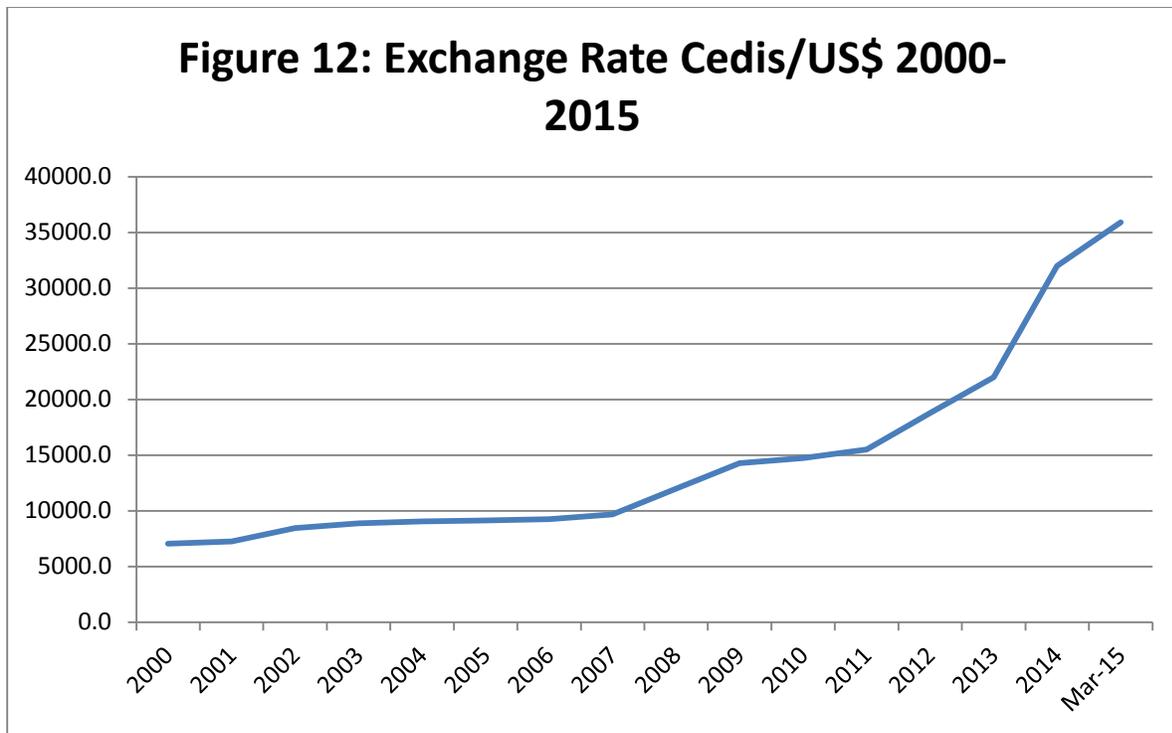


Source: Bank of Ghana

In terms of months of import cover, that was the lowest import cover for the NIR since 2000 and the lowest for any middle income or oil producing country in the world. At the end of 2014, and also as a result of the \$1 billion Eurobond proceeds and the cocoa syndicated loan, Ghana's net international reserves cover had improved to 2.2 months of import cover². This shoring up of foreign exchange reserves through borrowing from the international capital market is not sustainable. It is like when a guy borrows his friend's car to impress a girl he has met. She may be initially impressed but very soon his friend would come for his car and the girl will find out that he does not actually own a car! It is not a sustainable strategy.

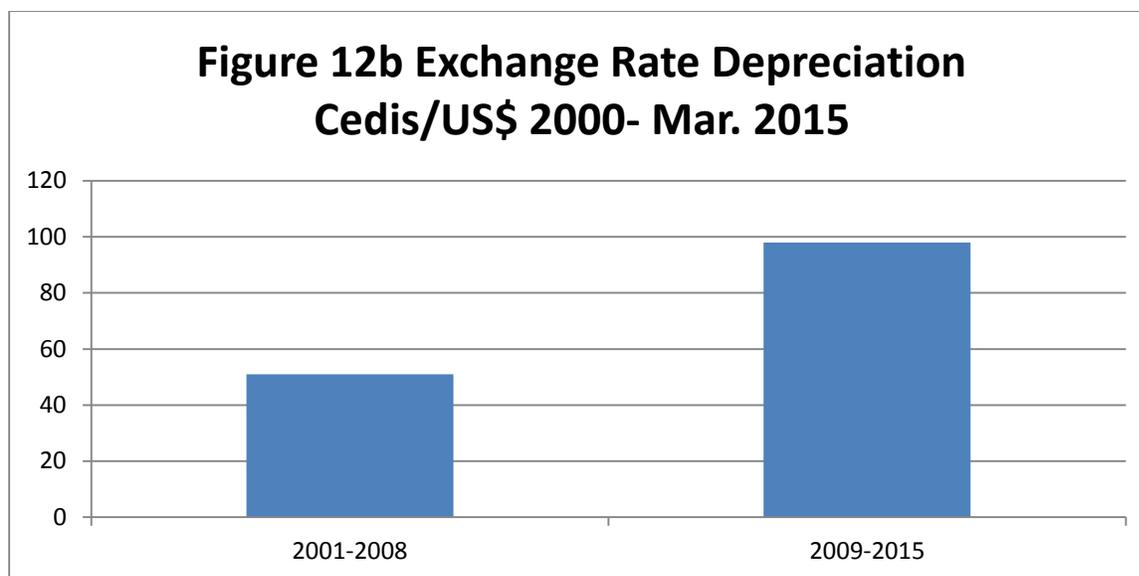
Mr. Chairman, in response to the deterioration of the external payments position, the exchange rate of the Ghana Cedi has also depreciated sharply following the expansive fiscal and monetary policy stance (Figure 12).

² Bank of Ghana Monetary Policy Committee, February, 2015.



Source: Bank of Ghana

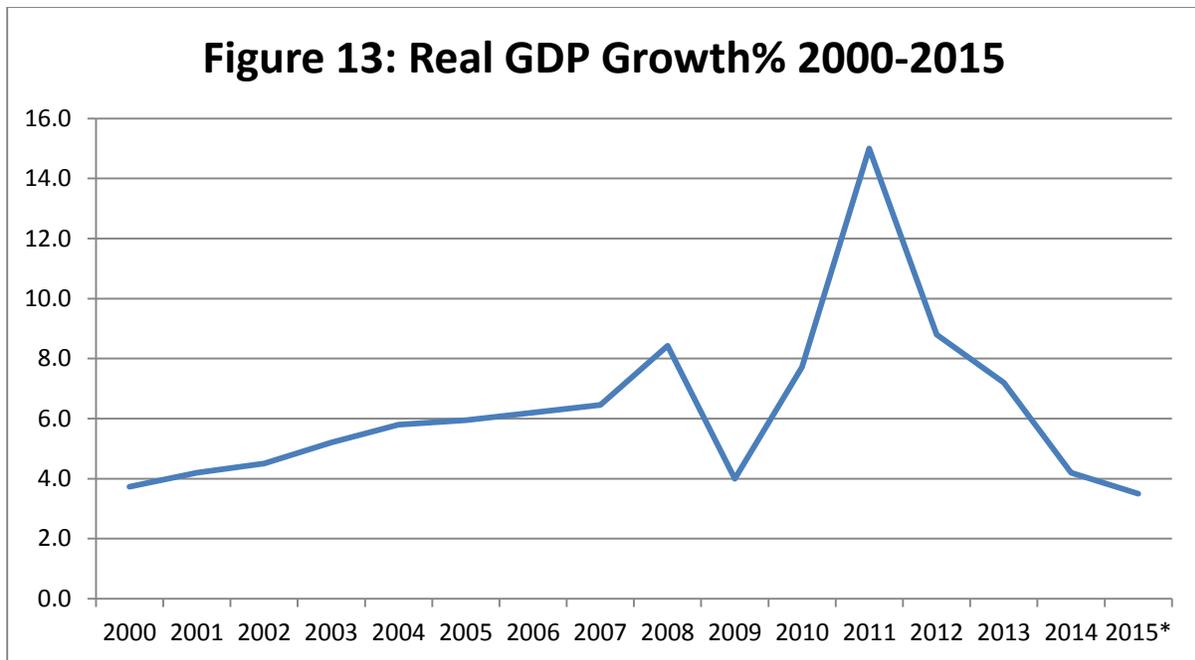
In 2014, the Ghana Cedi depreciated by 31% against the US dollar, making it one of the worst performing currencies in Africa in 2014. The depreciation of the cedi has continued in 2015, with an 11% loss in value between December 2014 and March 2015 thus far. Between 2001 and 2008, the cedi depreciated cumulatively against the US dollar by 51% in eight years. Between 2009 and March 2015 so far, the cedi has depreciated cumulatively by 98% after just six years (Figure 12b).



Mr. Chairman, on the financial sector, I would like to note that while the banking system has been described as generally stable, vulnerabilities remain. The weak economy and huge borrowing from government threatens stability. The entire financial system is at risk from rising non-performing loans (NPLs). Standard Chartered Bank for example, a well-managed bank, has seen its NPLs increase from 15.5% in 2013 to 27.3% in 2014. According to Stanchart’s financial statement for 2014, **“The increase is attributable to exposure of some of our customers to payment delays from government”**. The NPLs in the non-Bank sector in particular is becoming explosive and the Bank of Ghana has signaled that it may soon review capital requirements for the entire system.

Growth is Fast Declining

Mr. Chairman, another major reason why Ghana has requested an IMF bailout is because the economic growth in the country is on a steep decline. Real GDP growth has declined from 15% in 2011 (with the onset of oil production) to a projected 3.5% in 2015 (including oil) – Figure 13. The decline in economic growth is reflected across all sectors (Agriculture, Industry and Services). The 2015 budget is projecting non-oil growth of 2.7% in 2015. These facts are as revealing as they are disturbing. The growth rate in 2015 would be just about what it was in the year 2000 and half the rate of the 8.4% achieved in 2008 without oil! Non-oil growth in 2015 will be below the growth rates attained in 2000. When growth is declining this sharply, government revenue targets would also be compromised relative to expenditure and budget deficits would increase.



With the decline in economic growth, it is not surprising that unemployment is on the rise. Job creation is the ultimate measure of success of economic policy. No matter what a government does, no matter the statistics and no matter the projects any government can claim, if at the end of the day, graduates and the youth in general cannot find jobs to build their lives, then all those claims are pointless. If at the end of the day, economic policy leaves millions unemployed and with no hope of finding jobs, then the government would have failed the country and especially the youth.

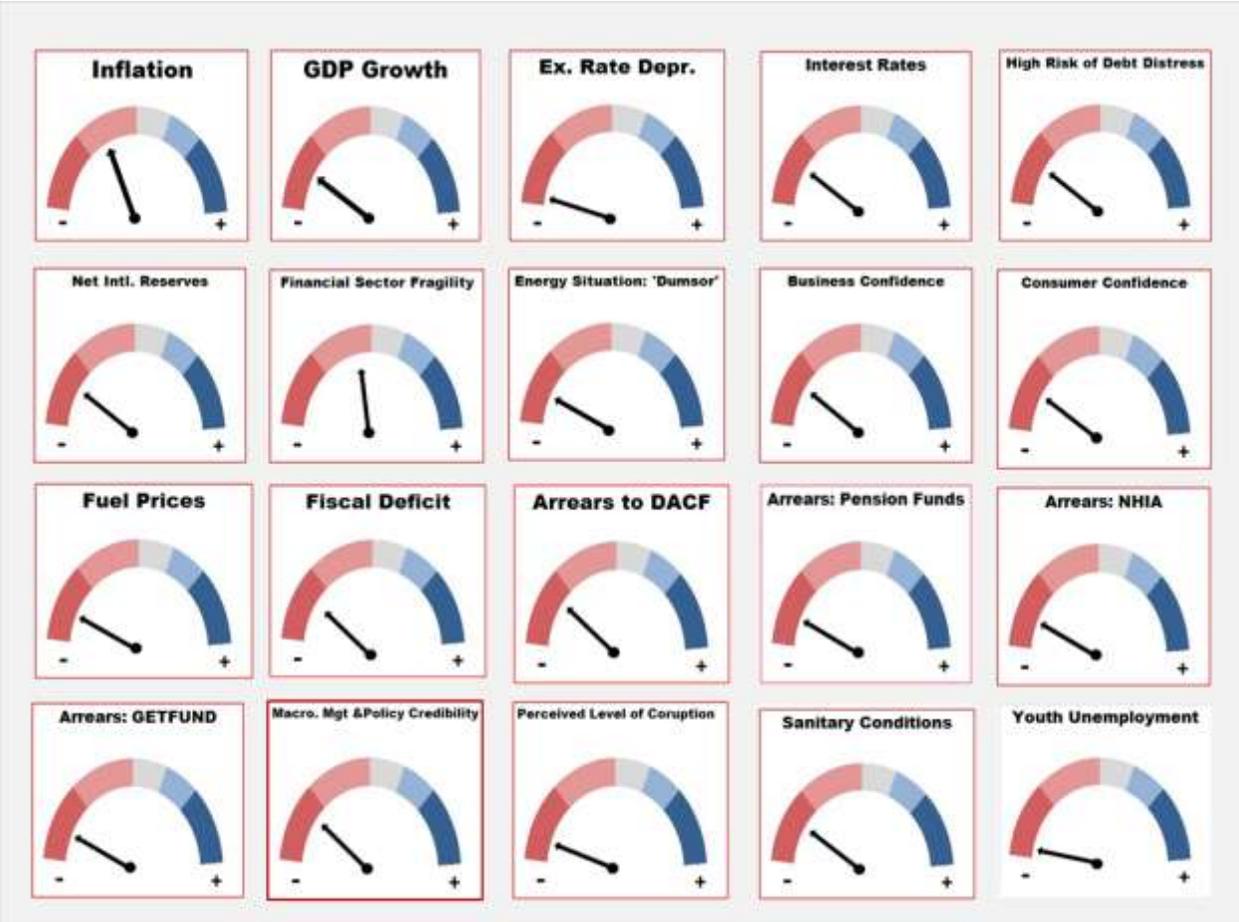
Figure 13b is a summary of the health condition of the Ghanaian economy, an Economic Odometer. It indicates that the economic conditions are for the

most part in red (bad). Ghana is in a bad state of economic health. As at August 2014 when the Government asked for the IMF bailout, the economy was characterized by:

- Declining Real GDP Growth
- Rising Cost of Living
- Depreciating exchange rate
- Declining Net International Reserves.
- Increasing Financial Sector Fragility
- Deteriorating Energy Situation- Dumsor
- Rising Interest Rates
- High Risk of Debt Distress
- Declining Business Confidence
- Declining Consumer Confidence
- Increased Fuel and Utility Prices
- Large Fiscal Deficits
- Arrears to DACF
- Arrears to GETFUND
- Erosion of Policy Credibility of Government
- Increasing Perceived Corruption
- Arrears to Pensions
- Arrears to NHIA
- Worsening Sanitation
- Rising Youth Unemployment, and
- Double digit current account deficits

All these negative developments point to the fact that Ghana has squandered the opportunities offered by HIPC debt relief and the oil discovery and in the process government has lost policy credibility..

FIGURE 13 (b). ECONOMIC ODOMETER



Notwithstanding these adverse developments government continued to insist that we were only going through a few challenges. They refused to admit that we were in a crisis. After a period of dithering, the government finally faced the reality of its inability to meet its obligations on a sustainable basis by opting for an IMF bailout in August 2014. Even when the decision was made, there was a reluctance by government to admit it. Government ministers explained variously that it was not a bailout but rather “technical assistance”. Government also explained that Ghana was this time around going to the IMF with its own conditions and could thus not be dictated to by the IMF. This left many people confused. If you have your own program to implement why would you need the IMF to come and implement it for you? How can one be seeking bailout from an institution and be setting the conditions it wanted to follow?

But just as with pregnancy that cannot be hidden for nine months, when the crisis finally became unbearable, government requested for an IMF bailout. Government admitted that it needed the IMF bailout not only for the money, but more importantly for policy credibility. Unfortunately, because of the delay in taking the decision for an IMF bailout, Ghana entered the negotiations in a very weak position. This drawn out negotiation was concluded with the IMF staff in February 2015 and is awaiting Board

Approval in April 2015. Following the conclusion of negotiations, the IMF announced that³ :

“ The main priority of the program is to restore debt sustainability through a sustained fiscal consolidation and to support growth with adequate capital spending and a reduction in financing costs. The program rests on three pillars-

- restraining and prioritizing public expenditure with a transparent budget process,**
- increasing tax collection, and**
- Strengthening the effectiveness of the central bank monetary policy”⁴ .**

Mr. Chairman, this statement is very revealing regarding the IMF’s assessment about the state of the economy. The IMF view inter alia is that:

- Ghana’s debt is unsustainable
- Financing costs are too high
- Capital spending is inadequate to drive growth
- Public expenditure levels are too high

³ The views expressed following the conclusion of negotiations are those of the staff and not the Executive Board of the IMF

⁴ IMF Mission Statement. Press Release No. 15/76. Accra February 26, 2015

- Tax collection is on the low side relative to expenditure
- The Bank of Ghana's monetary policy is not effective

Does this sound familiar?

WHAT ARE THE CONDITIONS FOR THE IMF BAILOUT?

Mr. Chairman, following the negotiations, the IMF agreed to provide Ghana with \$940 million Extended Credit Facility (ECF) over a three year period (2015-2017) provided the Government of Ghana meets certain conditions. Like a doctor dispenses medicine according to the diagnosis of the ailment, the IMF would set conditions for the loan that are in line with its diagnosis of what is ailing the Ghanaian economy. From statements of the government as well as the IMF (including recent IMF staff assessments), the type of focused conditionality under similar ECF and other programs in Zambia, Tanzania, Jamaica, Grenada, etc. and reading between the lines, one can surmise that the key conditions for the bailout program would include the following:

1. To restore debt sustainability, the policy prescription is to achieve this through “**sustained fiscal consolidation**”. This basically means that government would have to reduce its fiscal deficits over time (from 9.5% of GDP in 2014 to 3.5% of GDP by 2017). There is no debt relief available as was the case with HIPC and so there can be no reprieve from debt repayments.. This time around Ghana will have to bear the burden of adjustment itself. In 2015 for example the agreement is to reduce the fiscal deficit from 9.5% to 7.5% of GDP. This is to be achieved through:

- Expenditure Cuts, including cuts in capital expenditure
- Increases in tax collection
- Elimination of government subsidies e.g. on utilities.
- Measures to eliminate ghost workers on government payroll

Mr. Chairman, in my lecture last year and even in 2013, when I identified the high fiscal deficit as a problem, the government would not listen. Today because it is the IMF offering the same assessment, the government response is “Yes **Sir Massa we agree with you**”

2. The government would as part of fiscal consolidation, have to reduce its borrowing and accumulation of debt. When some of us made this recommendation last year, the President responded that the government would even borrow more because they were not borrowing to drink tea! Today because it is the IMF offering the solution as a condition, the government response is “Yes **Sir Massa we agree with you**”

3. To give legal backing to the process of fiscal consolidation, the government is likely to be required by the IMF to pass a Fiscal Responsibility law. A Fiscal Responsibility law will require governments to declare and commit to a fiscal policy that can be monitored. It will include fiscal rules and provisions for transparency and sanctions.

Mr. Chairman, in my lecture here last year and earlier in November 2013 when I delivered a lecture to mark the anniversary of the passing of Ghana's Former Vice-President, Alhaji Aliu Mahama, I offered this same piece of advice to government but the Minister of Finance responded that it was not necessary. Today because it is the IMF offering the solution as a condition, the government response is “Yes **Sir Massa we agree with you**”

4. To prevent the runaway printing of money by the central bank to finance the large deficits of government, the IMF is requiring that Bank of Ghana reduces its lending to government to zero by 2016. This means that in 2016 (the election year) the Bank of Ghana would not be allowed to lend any money to government.

Mr. Chairman, in my lecture last year, when I advised that the central bank was printing too much money to finance government, the Bank responded that it was not the case. Today, because it is the IMF offering the same assessment, the government has agreed with it.

5. As the IMF has stated, government would be required to remove all subsidies on utilities and petroleum products. This will cause increased hardships.

The removal of subsidies will also mean a strict implementation of the automatic price formula for utilities and petroleum products. Mr. Chairman, many in civil society as well as the minority political parties have criticized government for not applying the automatic adjustment formula for petroleum products, especially given the global decline in oil prices. The government

has refused to listen. Today, because it is the IMF offering the solution as a condition, the government has agreed with it. For , I would like to urge the government to publish all the elements of the automatic price formula so that we can all monitor.

6. Government has also apparently agreed to begin the rationalization of public sector staff through a combination of worker layoffs and voluntary retirements. My understanding is that government wants the IMF agreement to delay the worker layoffs until after the 2016 election. I wonder why? I suppose the message is “**vote for me before I fire you**”.

Mr. Chairman, the Bank of Ghana, especially last year, cast doubt on its ability to competently manage the foreign exchange market following the hastily announced foreign exchange control measures which virtually confiscated the foreign exchange deposits of firms and individuals. These measures, which were later reversed after they had proved counterproductive, if anything, worsened the plight of the cedi and undermined confidence in the Central Bank and the Ghanaian financial sector generally. In this regard the IMF has signaled that it would be

introducing reforms to make the foreign exchange market more efficient and transparent. To achieve this:

7. There would have to be a transparent quotation of exchange rates by the Bank of Ghana to reflect market conditions. This would make sure that the Bank of Ghana does not manipulate exchange rates in such a way as to create a major divergence between the Bank of Ghana rates, forex bureau rates and interbank rates.

8. Mr. Chairman, I also understand that the Bank of Ghana may be required to eliminate the compulsory surrender requirements of foreign exchange by exporters. Gold exporters for example will no longer be required to surrender their foreign exchange to the Bank of Ghana.

Mr. Chairman, this potential reform makes me a little nervous because I am not quite sure we are ready for this. However, I would much rather trust the foreign exchange market to allocate foreign exchange efficiently than the sort of exchange rate management that we witnessed in 2014 by the Bank of Ghana. One downside of this potential reform is that since most exporters bank with just a few banks, the foreign exchange market would end up being dominated by just a few banks. If indeed, it is true that this reform is being

introduced, then I can only hope that the Bank of Ghana is much better informed than the rest of us because if they get it wrong, we would see more depreciation of the cedi this year.

WILL THE IMF BAILOUT ANCHOR HOLD?

Mr. Chairman, the big question is whether the IMF bailout would provide the anchor necessary to propel Ghana's economy on a path of sustained growth and prosperity. If the program is successfully implemented as designed, it should restore macroeconomic stability, policy credibility, investor confidence and unlock donor funds. However \$940 million is not a lot of money over three years (an average of about \$313 million per year). It is the equivalent of the building cost of three Kumasi markets under this government's pricing. We should recall that the government issued a US\$1 billion sovereign bond in 2013 and that was not sufficient. The government issued another US\$1 billion in 2014 and that was not sufficient. So what difference would US\$313 million a year make?

The IMF would however provide us the analytical rigor that is presently lacking in the economic management space as evidenced by the policy

failure that has led us to seek an IMF bailout. It is clear that an analytical anchor is very much needed.

Mr. Chairman, what we should all recognize is that economic policies and the responsibility for their implementation is ultimately that of government. The IMF can design the best policy framework for you and if you mess up in the implementation, the country can end up in a mess. The IMF bailout is meant to restore macroeconomic stability through fiscal consolidation. Experience has shown that the IMF policy framework can provide an anchor for macroeconomic stability but in the case of Ghana at least governments have usually pursued policies that have returned the country onto a path of macroeconomic instability for electoral gain. At the end of the day we have to do it ourselves.

- Dealing with corruption is key to our development. However, the IMF cannot stop the corruption such as those associated with Woyome, GYEEDA, SADA, SUBAH, etc. if the political will to do so is not there. We have to do it ourselves.
- The issue of National ID cards for the population is very important. However, the IMF would not tell you to issue National ID cards even

though this is very critical to growth and development. We have to do it ourselves. Why can't we issue national ID cards seven years after the National Identification Act was passed?

- Mr. Chairman, financial inclusion is also a key pillar for development. Too many Ghanaians do not have a bank account. Without this, there would always be insufficient savings in the financial system. But the IMF would not tell you to make sure most of your citizens have bank accounts. We have the technology to change this within a year. We have to do it ourselves.
- As a country, the benefits of moving from cash-based economy to an electronic payments based one are enormous. The IMF would however not tell you to move towards electronic payments and away from a cash economy. We have to do it ourselves.
- Economic transformation and job creation should be at the heart of any economic strategy for Ghana. However, the IMF bailout would not provide us a path towards economic transformation and job creation. We have to do it ourselves.

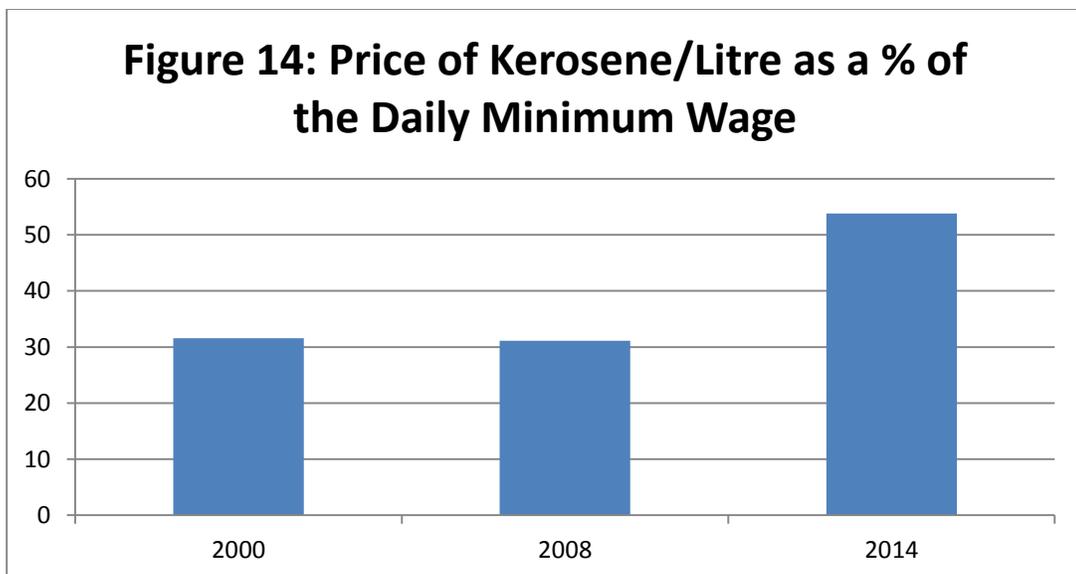
- Tax policy is very important in providing incentives to the private sector. The IMF bailout will however not tell you that in fact, you can increase tax collection by reducing taxes strategically. For example the marginal tax rates were reduced from 32.5% in 2003 to 25% by 2007 and yet government had higher tax revenue. We have to do it ourselves.
- Mr. Chairman resolving the current energy crisis is so critical for economic growth. However, the IMF will not tell you how to resolve “dumsor” (power outages). It will not tell you not to sign a 10 year emergency power deal to address a two year problem. It will also not tell you to wait for three years of dumsor before looking for an emergency solution. The government’s approach to the delivery of emergency power from Turkey or General Electric does not reflect the seriousness of the power situation. As I speak today, my understanding is that the Turkish power barges had not left Turkey as of last week and so the promise that they will be here to deliver power in April is not likely to be met. The IMF cannot do this for us. We have to do it ourselves.

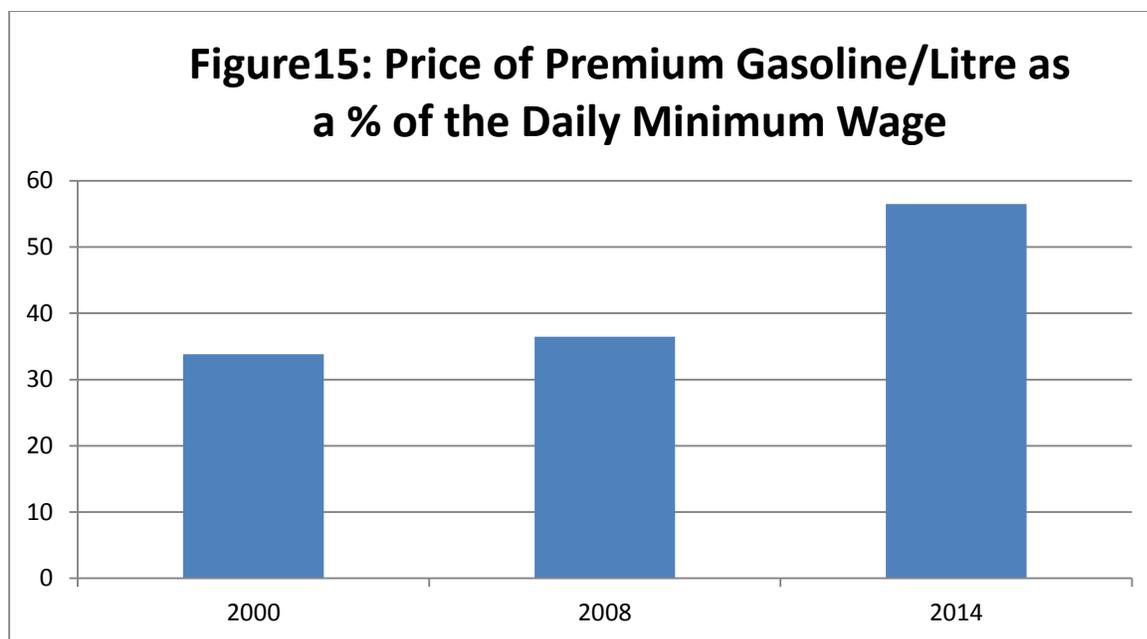
- Mr. Chairman, agriculture holds the key to our economic transformation. However, the IMF program will not tell you to pay attention to agriculture. We have to do it ourselves.
- Mr. Chairman, an IMF program does not guarantee fiscal discipline. Only a commitment to fiscal discipline by the government can guarantee it. Zero central bank financing is certainly new territory for Ghana. Will this government be disciplined in an election year (2016)? Most analysts are rightly skeptical. Notwithstanding the bailout agreement with the IMF, on March 20, 2015 Moody's downgraded Ghana's credit rating further into 'junk' territory (to B3) with a negative outlook. This is six levels below investment grade and signifies high credit risk. This means that investors are not yet convinced about the prospects for the economy even with an IMF bailout. Ghana would have to do a lot to convince the markets that it is committed to the program. It is in this regard that the announcement last week that Ghana was seeking new bridging loans of up to \$1.5 billion was quite shocking. It demonstrates a lack of understanding or appreciation of Ghana's debt dynamics by the government. How can the government be seeking to contract this magnitude of non-concessional loans at this

time when it does not have enough cash to meet statutory payments? This is like an alcoholic who has just been convinced to enter rehab and just a few days before rehab asks for a carton of whisky! Can this person be trusted to stick with the rehab program? Undertaking this additional borrowing would mean that the anchor is not likely to hold as it would compromise the objective of fiscal consolidation and debt sustainability. Given Ghana's economic situation, this bailout program will require a commitment to fiscal discipline that will test the resolve of any government in a developing country such as ours and it is important that the government understands what it has signed up for. We should collectively be prepared for some painful adjustments.

- Mr. Chairman, this IMF bailout would require that wage increases are very minimal if the targets are to be met. How understanding would labour be as the austerity program bites? If labour demands higher wage increases to compensate for the increase in austerity, the program targets for fiscal consolidation may not be met. Workers are already suffering from increases in prices of petroleum products, utilities, goods and services, layoffs (the Industrial and Commercial Workers Union is expecting some 2000 workers to lose their jobs by

June as companies cut back or shut down due to the high cost of doing business) and the effects of dumsor, etc. Take the increase in petroleum prices as one example. Figures 14 and 15 shows the price of Premium Gasoline and kerosene as a percentage of the daily minimum wage between 2000 and 2014.





By 2014, the price of kerosene and premium petrol per litre, relative to the daily minimum wage, was almost double that in 2000 and 2008. Furthermore, the 2009-2014 period has seen an almost doubling of the change in these product prices as a percentage of the increase in the minimum wage compared to the 1992-2000 and 2001-2008 periods. It is therefore clear that workers are being squeezed. How much more austerity can workers take?

If expectations are not well anchored, the success of the program would be compromised. Most Ghanaians have no idea how difficult the adjustment to this bailout program is going to be and this is partly because Government continues to paint a rosy picture.

CREDIBILITY OF THE DATA

Mr. Chairman any economic and financial program is only as good as the data used to formulate the program. Credible data provides the basis of the analytical framework to respond adequately to economic challenges. If you have make-believe data you will end up with counterproductive or inadequate responses to economic policies. If your data is not credible, the anchor cannot hold. With make-believe data as the basis, the best you can achieve is make-believe results which will soon be exposed as we are witnessing currently. I would like to examine the two most critical pieces of data underlying the IMF program, GDP and Inflation. This data is produced by the Ghana Statistical Service (GSS).

Mr. Chairman, credibility and reliability of key data like GDP and inflation is important because:

- If the inflation and GDP data are wrong, the inflation targeting framework will not work. The Monetary Policy Committee (MPC) may end up reducing interest rates when in fact they should be increasing interest rates.

- If the inflation and GDP data are wrong, then fiscal consolidation targets would be wrong. Goals of debt sustainability may only be achieved on paper. A higher GDP estimate than is the case would lead to an overestimation of revenue. Expenditure based on this overestimated revenue will result in budget deficits as the revenue would not be realized.
- If the inflation and GDP data are wrong, then there will be a disconnect between statistics and reality
- If the inflation and GDP data are wrong, then there will be a breakdown in the expected relationships between economic variables: e.g. inflation and depreciation, inflation and interest rates
- The bottom line is that the anchor will not hold if it is built on straw.

The GDP Data is Not Credible

Mr. Chairman, when the 2015 budget was announced, I had the opportunity to point out that the purported growth of real GDP by 6.9% in 2014 was not credible. How can an economy which went through so much turmoil in 2014, with a 31% depreciation of the currency and massive load shedding register real GDP growth of 6.9% only to decline sharply to 3.9% in 2015 when the government claims the economy is in recovery? The Ghana Statistical Service (GSS) subsequently revised the real GDP numbers⁵. These revised numbers are however still very problematic and the Ghana Institute for Fiscal Studies (IFS) has recently pointed out these anomalies.

The revised GDP 2014 estimates (reproduced in Table 1 below) shows growth rates of non-oil GDP at 2006 constant prices. The Table contains some curious data. How can agriculture grow at 7.2%, industry at 4.5% and services at 5.6%, but then overall GDP at basic prices grows at 2.2%?

The GSS also revised the estimates for net indirect taxes (in constant terms). Curiously, however, real growth rates for net indirect taxes are equal to real growth of GDP at basic prices for all the years since 2009 (Table 1). We expect the growth of indirect taxes to correlate with the growth of GDP

⁵ Revised Gross domestic Product 2014. Ghana Statistical Service, January 2014

at basic prices, not to be equal all the time (Table 1).

Table 1: Growth Rates of Non-Oil GDP at 2006 Constant Prices						
	2009	2010	2011	2012	2013	2014
Agriculture	7.2	5.3	0.8	2.3	5.2	5.2
Industry	4.5	5.6	16	8.5	3.6	3.5
Services	5.6	9.8	9.4	12.1	10.3	4.1
GDP at basic prices	2.2	7.6	8.2	8.6	6.7	4.1
Net Indirect Taxes	2.2	7.6	8.2	8.6	6.7	4.1
GDP at Purchasers values	2.2	7.6	8.2	8.6	6.7	4.1

Mr. Chairman, comparing the GSS net indirect taxes at constant 2006 prices data to the figures in the 2015 budget appendices, for the same data (reproduced in Table 2 below) is interesting. The Ministry of Finance is the custodian of indirect tax data; its figures should not differ from the GSS, but that's the case we have here. Where did the GSS get their data from? The GSS needs to explain these anomalies in the data.

Table 2; Net Indirect Taxes: GSS and MOF

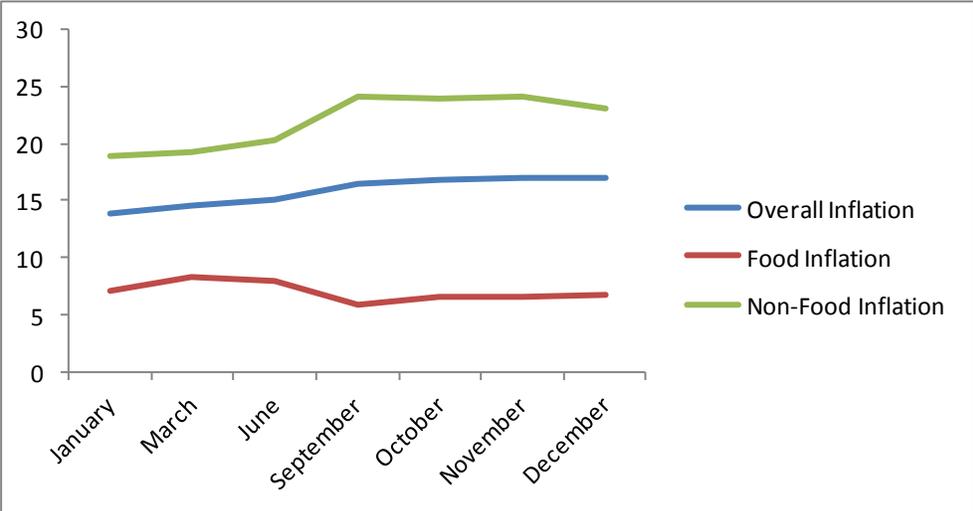
Year	Net Indirect Taxes at Constant 2006 Prices - (GSS)	Net Indirect Taxes at Constant 2006 Prices - (MoF)
2009	1,554.00	1,672.40
2010	1,677.00	2,654.40
2011	1,913.00	3,964.50
2012	2,090.00	2,532.90
2013	2,244.00	2,714.10
2014	2,338.00	2,840.20

The GSS Inflation Data is Suspect

Mr. Chairman, the data on inflation produced by the GSS does not appear to reflect actual price developments. I have raised this issue before and I have returned to it today with further and better particulars. The year 2014 was a very bad one as far as the economy is concerned. The exchange rate depreciated by 31%, utility and petroleum prices went up significantly and economic growth declined but for some reason inflation, especially food price inflation remained relatively subdued according to the Ghana Statistical Service. Between January and December 2014, the rate of increase in food prices as reported by the GSS actually declined marginally from 7.1% in January to 6.8% by December. Non-food prices on the other hand increased

from 18.9% to 23.9% over the same period. Overall inflation increased from 13.8% to 17% on account of the decline in food price inflation (Figure 16). Clearly, the supposed low rates and even decline in food price inflation accounted for the relatively low inflation figures reported by the GSS (Figure 16).

Figure 16 :Inflation Trends 2014



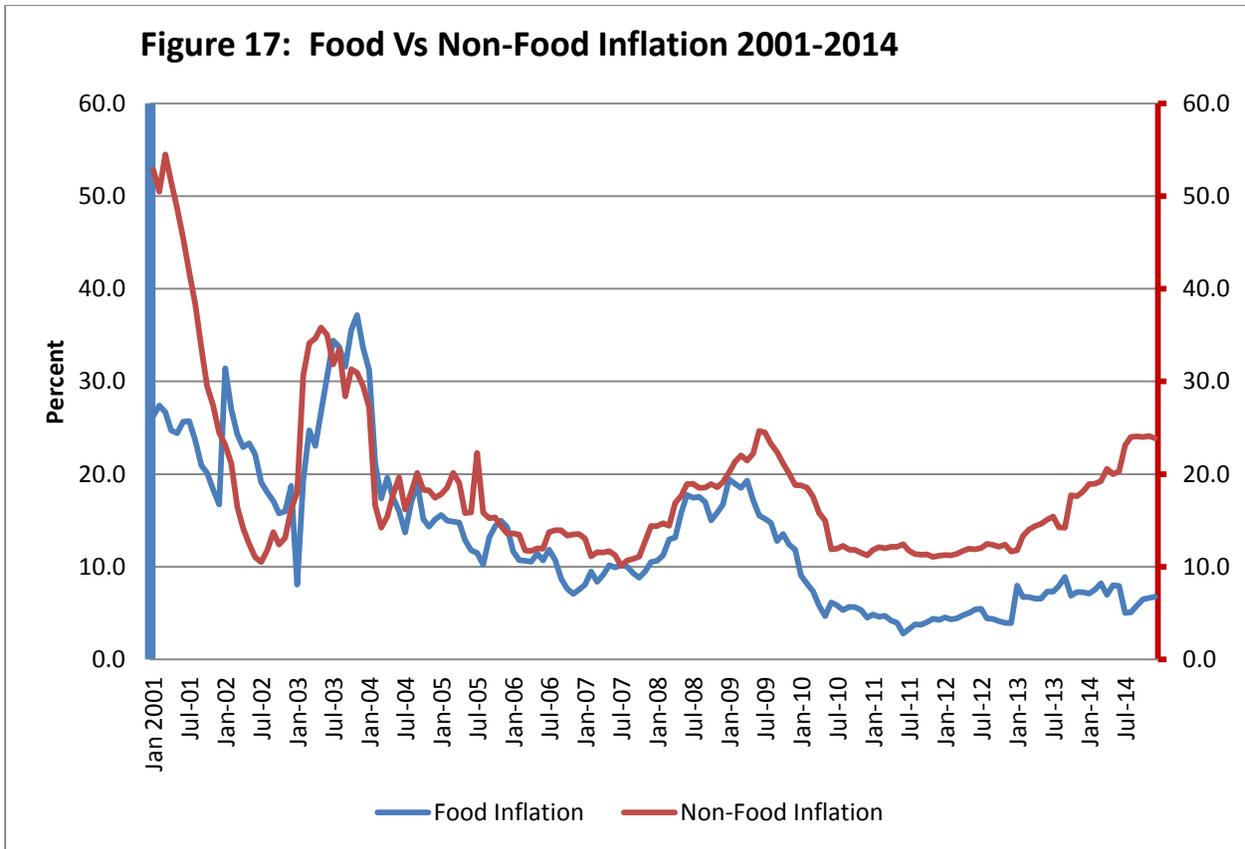
Mr. Chairman, the decline in food price inflation is a curious phenomenon worthy of further investigation because it defies evidence that suggests otherwise. Most people one has talked to cannot believe that food price inflation has declined. Market survey reports by Joyfm news (under the

heading “food prices killing Ghanaians”⁶ as well as the Finder news paper (under the heading “70% hike in food prices in just one year”) indicate very high increases in food prices⁷.

Mr. Chairman, figure 17 suggests a structural break in the relationship between food and non-food inflation since 2009. Between 2001 and 2008, the relationship was much closer. Why did the relationship start to drift apart and even move in opposite directions? Was there a deliberate attempt to keep inflation down by fixing low food price inflation?

⁶ <http://www.myjoyonline.com/business/2014/july-22nd/high-food-prices-killing-ghanaians.php#sthash.C2oTPSrD.dpuf>

⁷ <http://www.ghanaweb.com/GhanaHomePage/NewsArchive/artikel.php?ID=318014>



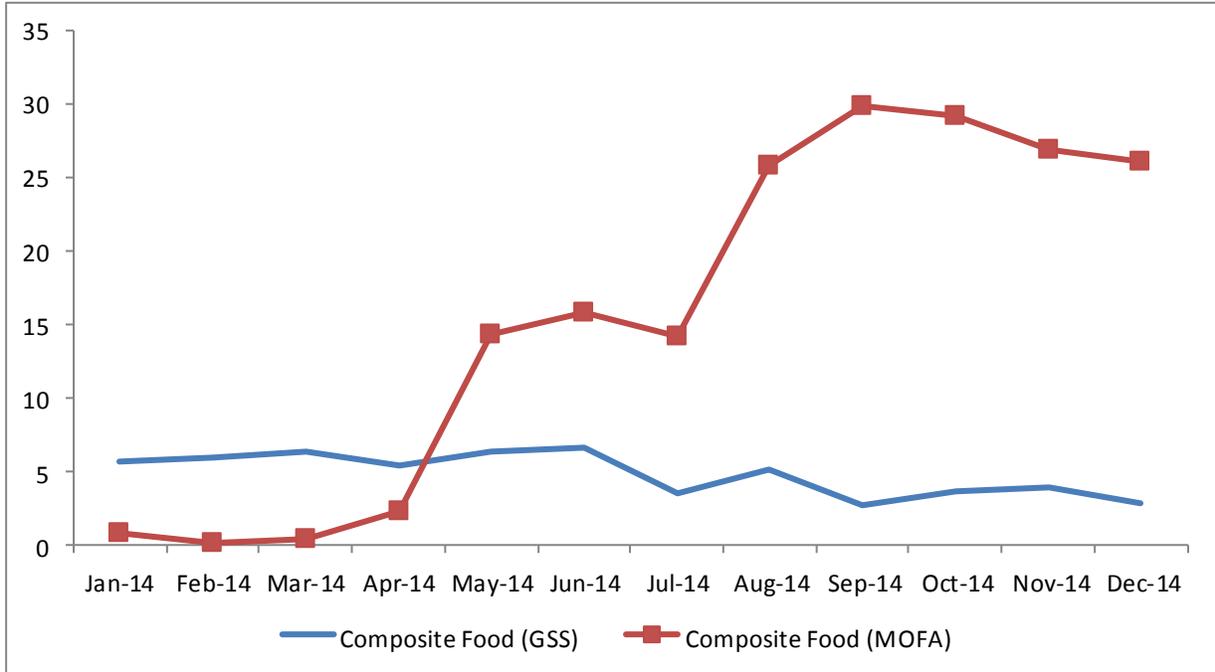
To conclusively challenge the GSS estimates however, one needs independent data for the individual food items in Consumer Price Index over the period. Thankfully, such data exists and has been collected by the Ministry of Food and Agriculture (MOFA) across all ten regions of the country and published by the Statistics Research and Information Directorate of MOFA.

Mr. Chairman, since the data was collected for the same commodities, and over the same period across the country, one would expect a close

relationship between the two sets of price data, especially since these are both government/state sources. Thus if we even decide to ignore all the experiences of the market women and others, who complain of sharp rises in food prices, we expect that at least, the figures of the Ministry of Food and Agriculture, should to a large extent corroborate the figures of the Ghana Statistical Service.

However, a comparison of the MOFA and GSS (both official sources) estimates of food price inflation overall and across specific food items shows very divergent estimates. Figure 18 shows that for 2014, while the MOFA estimated an increase in overall food price inflation from 0.7% in January to 26% by December 2014, GSS on the other hand estimated a decline in food price inflation from 5.7% in January to 2.8% by December 2014.

Figure 18: Food Price Inflation: GSS versus MOFA



Going to specific food items, the divergences are quite stark as well. A few examples will suffice in the charts below for yam, rice, oranges, maize, groundnuts, and smoked herrings (see figures 19-24 below). In all these examples (as with the composite) the inflation measured by the MOFA is significantly higher than the GSS estimates .

Figure 19 shows that for 2014, while the MOFA estimated an increase in yam price inflation from 0.6% in January to 8.4% by December 2014, GSS on the other hand estimated a decline in yam price inflation from 3.4% in January to -1.8% by December 2014.

Figure 19: Yam Price Inflation: GSS versus MOFA

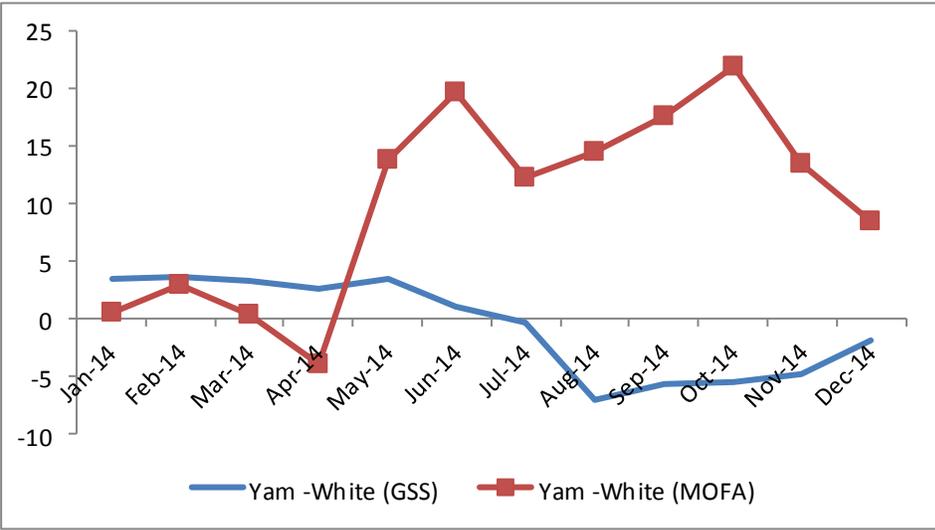


Figure 20 shows that for 2014, while the MOFA estimated an increase in rice price inflation from -2.3% in January to 5.2% by December 2014, GSS on the other hand estimated a decline in rice price inflation from 4.3% in January to -11.6% by December 2014.

Figure 20: Rice Price Inflation: GSS versus MOFA

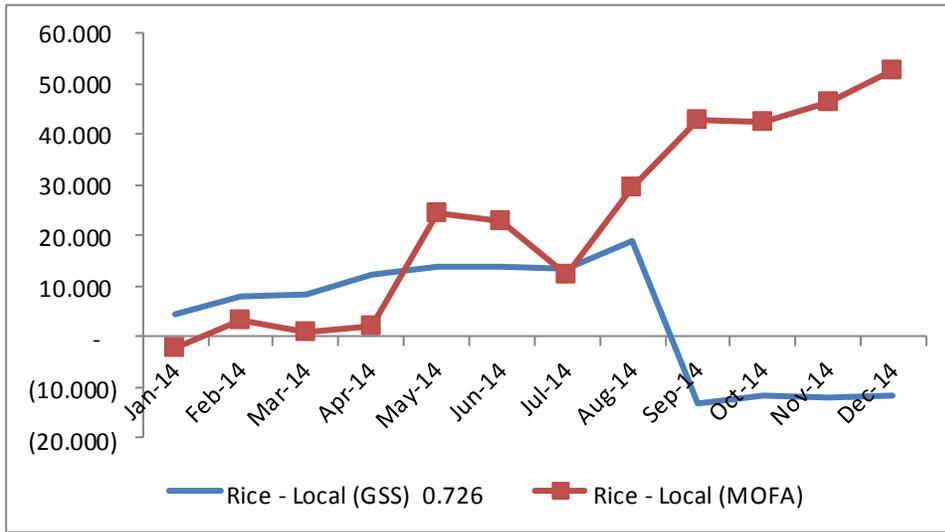


Figure 21: Groundnut Price Inflation: GSS versus MOFA

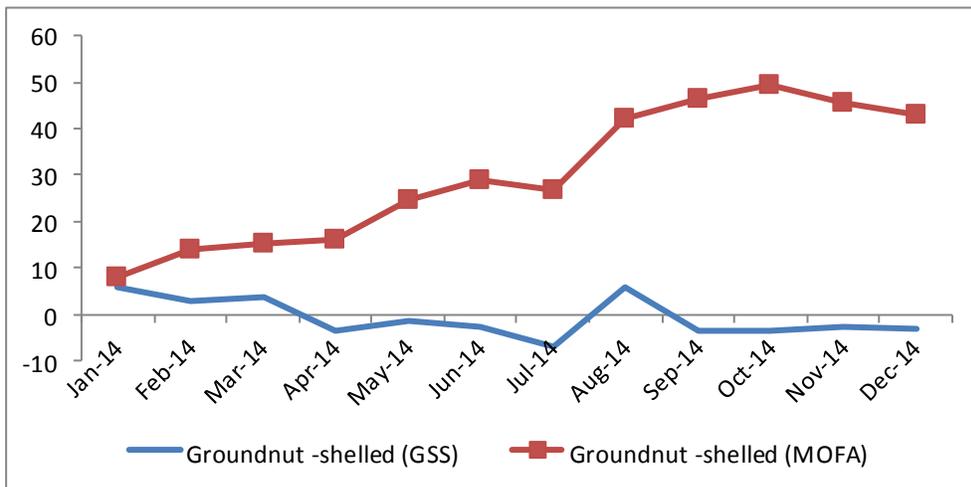


Figure 21 shows that for 2014, while the MOFA estimated an increase in groundnut price inflation from 7.8% in January to 43.2% by December 2014, GSS on the other hand estimated a decline in groundnut price inflation from 5.9% in January to -2.98% by December 2014.

Figure 22: Orange Price Inflation: GSS versus MOFA

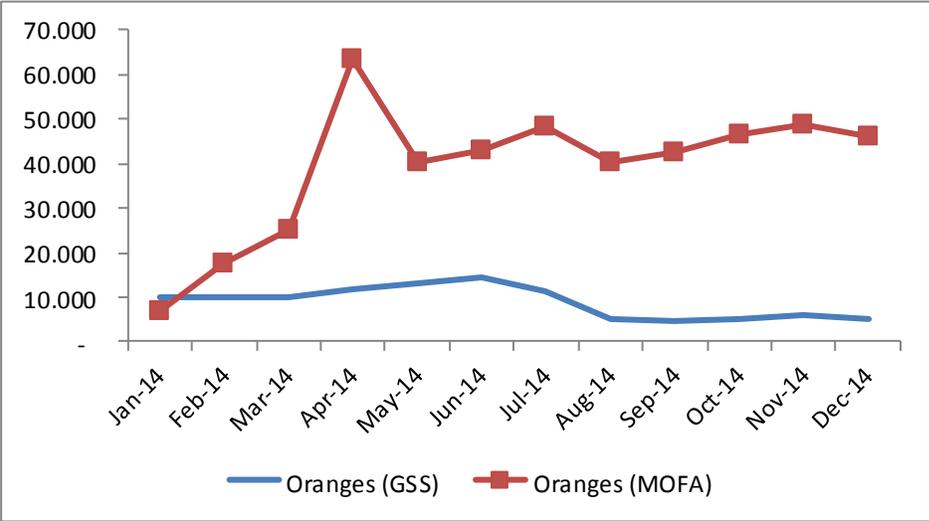


Figure 22 shows that for 2014, while the MOFA estimated an increase in oranges price inflation from 6.8% in January to 46% by December 2014, GSS on the other hand estimated a decline in oranges price inflation from 9.9% in January to 4.9% by December 2014.

Figure 23: Maize Price Inflation: GSS versus MOFA

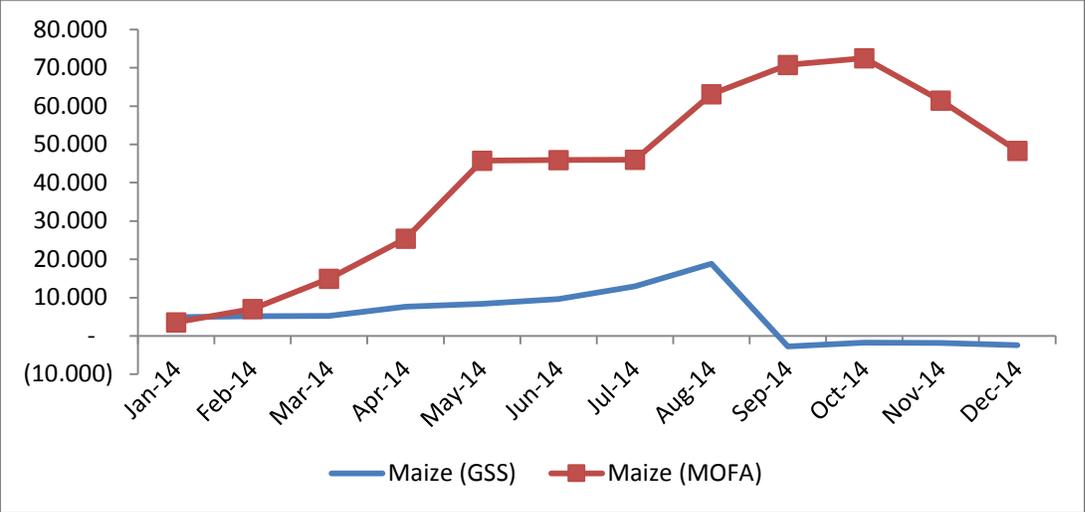
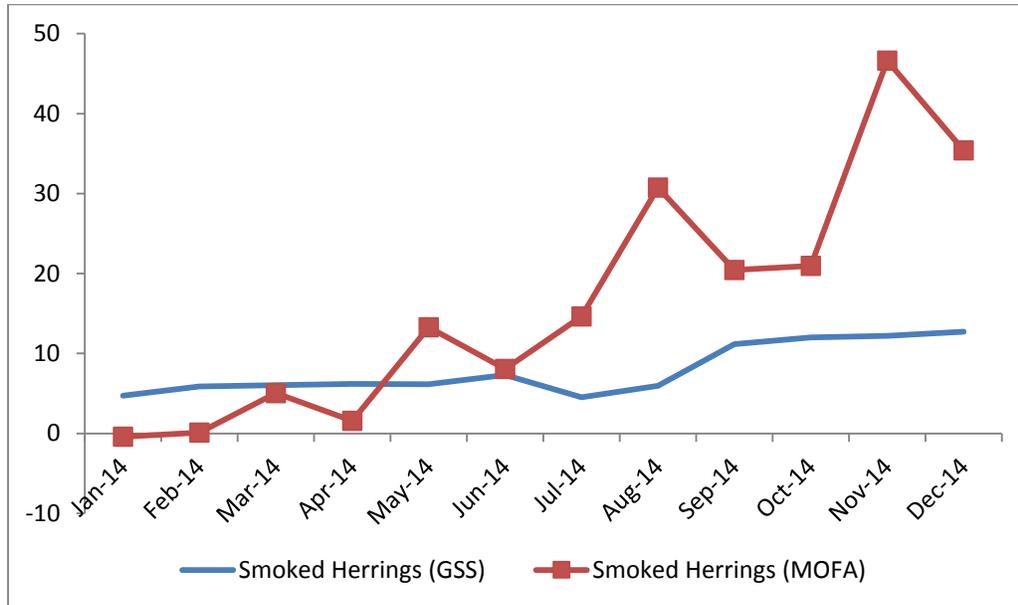


Figure 23 shows that for 2014, while the MOFA estimated an increase in maize price inflation from 3.5% in January to 48% by December 2014, GSS on the other hand estimated a decline in maize price inflation from 4.8% in January to -2.3% by December 2014.

Figure 24 shows that for 2014, while the MOFA estimated an increase in smoked herring price inflation from -0.4% in January to 35% by December 2014, GSS on the other hand estimated an increase in smoked herring price inflation from 4.7% in January to 12.7% by December 2014.

Figure 24: Smoked Herring Price Inflation: GSS versus MOFA



Mr. Chairman, the MOFA estimates appear more consistent with the observations and experiences of people than the GSS estimates. These are prices of the same food items in the same markets across the country. Why should there be such wide differences? The GSS needs to explain these anomalies quickly to continue to maintain the confidence of the public. At the end of the day, if the data is not credible, the anchor cannot be credible.

CONCLUSION

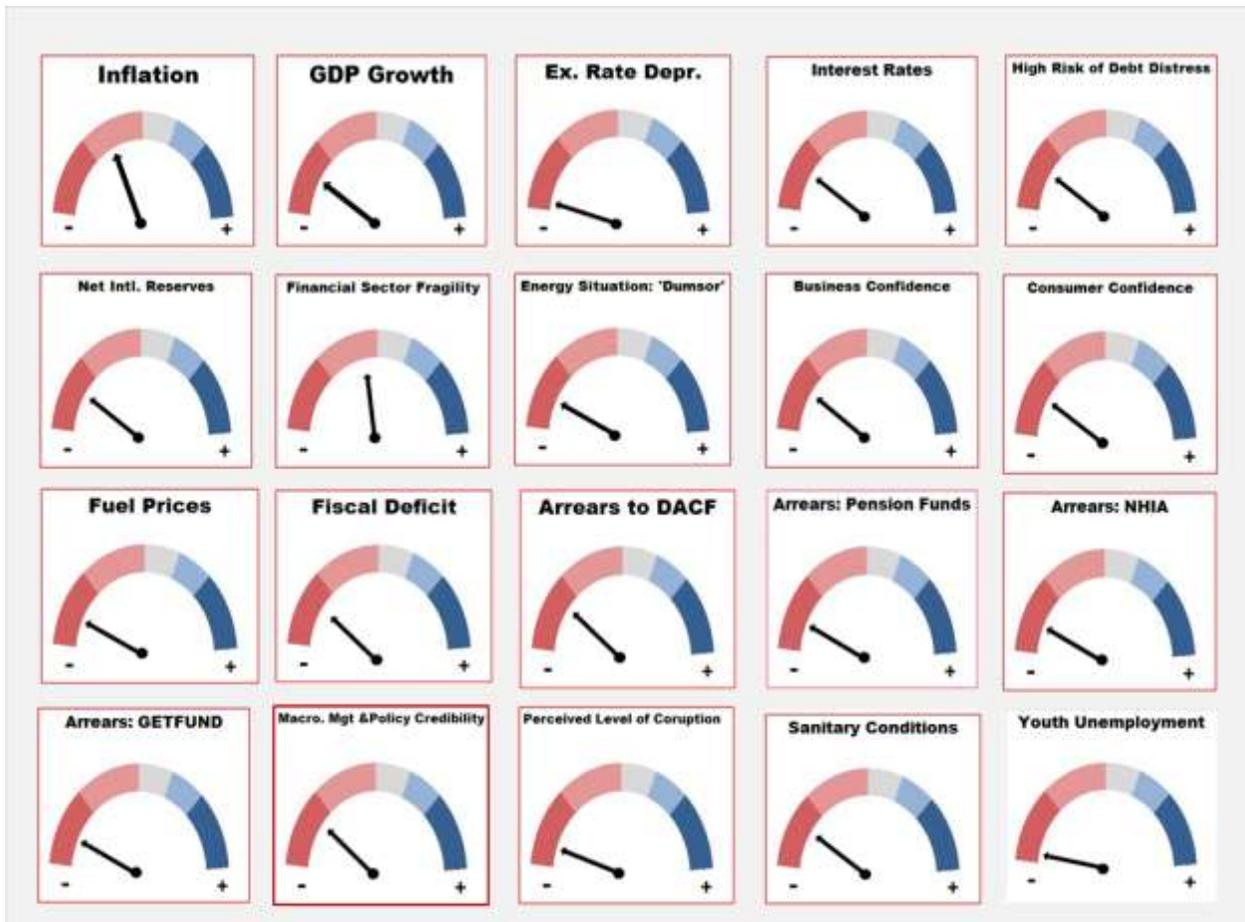
Mr. Chairman, the IMF bailout was totally avoidable if the government had listened to sound advice from many quarters much earlier. But government refused to listen. They believed in their own propaganda and said “Yentie Obiaa” (We won’t listen to anyone). When government was cautioned about the scale of borrowing, the government responded that they would borrow more. Now that their propaganda has been exposed by economic reality, they are now forced to listen to the IMF. We have moved from “Yentie Obiaa to “Yebetie IMF Nkoa” (we will listen to the IMF only).

Mr. Chairman, what is worrying is that the government is still unwilling to admit the reality that the policies pursued over the last few years harmed our economy. Government continues to rationalize and even justify these very policies that have landed us in the hands of the IMF with claims like “Smart Borrowing” still being pushed by the managers of our economy. With this thinking, it is hard not to be worried about whether these same managers of the economy will be willing or even able to oversee the significant changes required to turn the tide and return the economy to a healthy state.

Ghana has had many IMF bailouts before. Will the anchor hold this time? What is clear from our experience is that the anchor will have to be provided by the commitment of the government and people of Ghana to fiscal discipline and sound economic policies and not the IMF. Without this, the anchor will not hold. The anchor certainly will not hold if the GDP and inflation data on which the program is based is not credible. There are also many other issues that are outside the remit of the IMF (e.g. corruption, agriculture, National ID cards, financial inclusion etc.) which are critical for the anchor to hold.

Mr. Chairman, I believe that with hard work, dedication, integrity and sound economic policies, Ghana's brighter days are ahead of us. We can do it ourselves but as I continue to say, discipline and honesty remain the keys. We can change the current reading of the Economic Odometer from red to blue if we do the right things. Fellow Ghanaians, with good economic management and incorruptible leadership, we can do it ourselves.

FIGURE 13 (b). ECONOMIC ODOMETER



Thank you for your attention

God bless you

God bless our homeland Ghana