The Institute of Economic Affairs
A Public Policy Institute
IEA Ghana

Tuesday, 3rd April, 2024

IEA PRESS BRIEFING
REFLECTIONS ON THE SONA AND MPC STATEMENT

In the past month, two important national policy events took place. On 27th February, the President presented his State of the Nation Address (SONA) to Parliament. And then on 25th March, the Governor of the Bank of Ghana (BoG) presented the Monetary Policy Committee (MPC) Decision at a Press Briefing. As these two important events took place close to each other, we thought it would be more productive to wait to provide our views on them together, rather than separately. In any case, there were several overlaps in the two statements regarding performance of the economy and, therefore, they can be appropriately considered together.

I: THE SONA
Peace and Security
The President placed peace and security at the very top of his statement, and rightly so because without peace and security, no nation can make economic progress. The President was satisfied about the prevalence of peace in Ghana, which seems to be virtually an island in an otherwise troubled sub-region afflicted by civil and military strives and undemocratic regime changes. The President said this is something that Ghanaians should be proud of and guard strongly. Further, the President was hopeful about Ghanaians' commitment to multi-party democracy. He pointed in particular to media freedom being "guaranteed in the country." While, as he noted, the proliferation of FM stations and newspapers and the explosion of virtually unfettered social media space signify expansion of media freedoms, persecution of media personnel by state agencies is commonplace while "a culture of silence" is believed to prevail in the country.

Projects
The President recounted what he described as "numerous projects" undertaken by his Government, especially infrastructure projects, describing many of them as "unprecedented." Here, we know that pronouncements could differ from the reality on the ground. Also, it is not always easy to differentiate continued projects from new ones. To help resolve these contentions, the President promised to make available a "Project Performance Tracker" in March. As of today, 3rd April, we are not sure whether the Tracker has been released or not. The President also recounted the Government's many achievements in digitisation. This is an area where the Vice President, in particular, has been quite active, rolling out many initiatives, including in the areas of personal identification, digital addresses and economic and financial transactions. Digitisation is important as it brings about savings regarding time and space in carrying out our daily activities and, therefore, increases efficiency that translates into higher economic output and growth. Here also, the distinction between continued and new initiatives is not always clear.

Taxes
The President mentioned the introduction of many taxes by his Government "to address a difficult situation," describing them as "bitter, but necessary medicine." The proliferation of taxes has raised serious concerns among consumers and businesses. We, on our part, have argued that some of the taxes, such as E-levy, Covid Levy, Growth and Sustainability Levy, Sanitation Levy, and the aborted Emissions Levy, Betting Levy and VAT on electricity consumption, are multiple, nuisance or outdated taxes that cannot be justified. The Government must also be reminded that it came to power on the promise that it was going to move economic policy away "from taxation to production," which runs counter to what they have been practising. Further, we recognise the lack of

P. O. Box OS 1936, Christianborg, Accra, Ghana. Tel: +233 302 244716 / 226388 / 226333 / 030 7010713/4
Fax: +233 302 222313 | Email: iea@ieagh.org | Website: www.ieagh.org

equal effort on the part of Government to curtail its expenditure, including in respect of its size and numerous flagship programmes. The fiscal consolidation being implemented under the IMF program has to be even handed; it must fall equally on expenditure and not just taxes.

Debt

The President mentioned the restructuring of Ghana's debt for the purpose of reaching sustainability under the IMF program. He noted that the local component of the restructuring, i.e. the Domestic Debt Exchange Programme (DDEP), had "made significant progress." It seems progress here is being measured in terms of the degree of participation. However, we should not lose sight of the immense hardship the DDEP has brought on bond holders, including pensioners and the financial sector, which was heavily exposed to Government debt. Even BoG was not spared the adversity. The Bank suffered a heavy discount of its holdings of Government bonds, causing it to make a whopping historical loss and recording a huge negative equity in 2022. The attempt by both the BoG Governor and the then Minister of Finance to describe the Bank's loss as only "a technical loss" and, impliedly, inconsequential, was disingenuous, to say the least, as the loss had far reaching implications for the Banks's future operations. The bizarre thing is that, Government has racked up its borrowing from the domestic market as some of the external funding for the budget have stalled, raising the public debt once more and crowding out the private sector in the process. Here, we want to repeat our call for the imposition by Parliament of a debt ceiling of 60% of GDP in the Fiscal Responsibility Act in addition to the existing deficit ceiling to ensure permanent debt sustainability.

Macroeconomy

The President noted that the macroeconomy was stronger in 2023 than 2022, citing inflation, GDP growth, depreciation, reserves, and current account figures to illustrate his assertion. He added that the macroeconomic indicators were, once again, "pointing in the right direction." While his description of the macroeconomic situation in 2023 compared with 2022 was right, using 2022 as his base for comparison appears a bit self-serving. This is because 2022 saw record deterioration in many of the indicators. Indeed, the fact is that almost all the indicators were worse in 2023 than what the Government inherited in 2016. It is the case that the indicators generally improved during 2017-19 and worsened during 2020-22. The Government must be commended for the improved outcomes during 2017-19, which occurred on the back of both improved policies, including enactment and observance of the Fiscal Responsibility Act (FRA). Favourable exogenous conditions, such as stable oil prices, also played a positive contributory role. Government must, however, equally accept responsibility for the poor macroeconomic outcomes during 2020-22, which happened due to inappropriate policies, such as excessive spending, including on numerous flagship programmes, and excessive and expensive borrowing. While exogenous shocks, in particular Covid-19 and the Russia-Ukraine war, also played a negative role, they impacted the economy against the backdrop of existing vulnerabilities, which compounded Ghana's economic crisis.

Social Protection

The President mentioned Government's reinforcement of social protection schemes, such as LEAP, School Feeding and Capitation Grant. The fact, however, is that allocations to these schemes remain grossly inadequate and recipients remain economically vulnerable. School feeding, for example, allocates a mere GHS1.20 (equivalent to 10 US cents) to each pupil per day. This is not only peanuts but represents official insensitivity to the welfare of the pupils. To us, a reasonable feeding amount would be GHS6.00 (equivalent to 50 US cents). Additionally, we would recommend to Government to allow parents to contribute to the feeding of their wards so that Government can concentrate on other needs and be able to deliver them more effectively.

Free Senior High School

The President highlighted the importance of the Free Senior High School Policy (FSHSP) as a vehicle for increasing access to Senior High School and building human capital for the development of Ghana. He noted expansion in school infrastructure and facilities. The President, however, refrained from mentioning some of the shortcomings in the FSHSP, including in terms of congestion, poor feeding and inadequate facilities and supplies.

The call has been widely made for a review of the policy to address the associated lapses, a call that we associate with. In particular, capable parents—identified through the survey used to determine families eligible for LEAP or some form of means-testing—should be made to contribute to educating their wards so as to reduce the burden on the budget and to improve quality generally.

“Dumsor”

The President mentioned his Government’s success in ending the “DUMSOR” menace and managing “to keep the lights on in the last seven years.” We are not going to get into the unproductive debate as to who ended “DUMSOR.” The fact that power has been much more stable in the last seven years than the previous four years, however, is evidently clear. It is also a fact that the subsequent stability benefited from previous investments in the power sector. What we also know is that the stable power has been achieved at considerable budgetary cost some of which emanated from previous contractual agreements. Indeed, it is known that the energy sector is beset with huge cross debts. Undoubtedly, challenges in the energy sector prevail and need to be addressed holistically to stem the periodic outages. The solution should include how to deal with the legacy debts, improving efficiency of the Electricity Company of Ghana (ECG), including by reducing the industry-high distribution losses, improving bill collections, stemming illegal connections and moving to legitimate cost-recovery tariffs. Meanwhile, given inefficiencies in the current management of ECG, consideration should be given to recruiting expert managers, wherever they may come from, to manage ECG under state ownership.

PFJ

The President duly recognised the importance of national food self-sufficiency. He did not provide an assessment of the Planting for Food and Jobs (PFJ) programme that had driven Government’s agricultural policy for six years. PFJ.1 has been generally seen as not having improved the food situation as expected as food remains a huge item in Ghanaians’ budgets (44% of the monthly budget) and food security remains elusive. The President stated that based on lessons learnt from a review of PFJ.1, Government developed and launched PFJ.2 that sets out a 5-year strategy to “ensure food self-sufficiency and resilience,” with strategic targets set for eleven priority products. Not enough detail was provided on PFJ.2 for us to be able to make a full assessment of how much value it will add to PFJ.1 and whether it is capable of achieving the intended results. Our further investigations have revealed that the PFJ.2 would address more effectively the entire food chain from production to storage/preservation to marketing. It would also address the usual allied challenges regarding inputs such as seeds, fertilizer, credit and extension services, while catering to the requirements of both peasant and large-scale commercial farmers. These are challenges that have faced agriculture for decades, but have not been adequately dealt with. We are told PFJ.2 is designed to be holistic and more effective. Notably, targets have been set for the selected 11 priority products for the immediate term (September to December 2023), short term (year 2024), medium term (2025 -2026), and the long term (2027-2028). It should therefore make it easy for us to track the performance of the PFJ.2 going forward if adequate information is provided on the outcomes.

Minerals

The President mentioned a huge increase in the volume of Ghana’s gold production, taking the country back to the number one position in the world. It is also known that gold price is at a record high. Taking Ghana’s reported annual production of 4 million ounces and multiplying by the current world price of US$2,200 per ounce gives US$8.8 billion. The question, however, is: how much of this belongs to Ghana? Ghana’s share is not likely to exceed 20% or about US$1.8 billion, while the much bigger share of about US$7.0 billion goes to foreign companies. It is important for Ghana to assume ownership of its natural resource wealth to provide greater benefits to the country. This will require the signing of new contracts to give effect to this need. The President mentioned the construction of a local gold refinery to add value to the commodity. This policy is long overdue and should be extended to all of our natural and agricultural commodities. We should construct cocoa processing factories and refineries for oil, bauxite, lithium, etc., to take advantage of the vast difference between the prices of the refined products and the raw commodities.

<u>"Where the Buck Stops"</u>

The President clarified his responsibility as an Executive President vis-a-vis his numerous advisors, and emphasised that the buck stops with him. This statement was, ostensibly, meant to give credence to his Vice's recent assertion that he has been "a driver's mate" his entire tenure, implying that he could not be held directly responsible for the decisions made by the Government. While the President's affirmation may be intended to exonerate his Vice from the failings of the Government, and thereby boost his electoral chances, it runs counter to the way the President validated his choice of his Vice as his running mate in terms of his economic prowess and his subsequent position as head of the Economic Management Team (EMT), which has oversight responsibility for the economy. To us, admitting responsibility for the failings while claiming credit for the successes would rather boost the Vice's image.

<u>"Missing Pieces"</u>

The President could not have touched on every subject in his limited speech. Everybody will have their own views of what is important or not in a SONA. We would pick just two issues that we find to be key but conspicuously missing from the SONA. These are Corruption and "Galamsay."

<u>Corruption:</u>

Corruption is such an important issue in Ghana that it is inconceivable that the President would gloss over it. Local and international corruption reports indicate that no significant progress has been made in tackling the canker in the past 30 years or so. The menace remains endemic and pervasive. The problem with corruption is that it promotes private gain at public expense. Corruption enriches a few private individuals while it impoverishes the masses. This Government established the Office of the Special Prosecutor (OSP), ostensibly to act independently from the Attorney General (AG), who is inextricably linked to the Executive. However, the OSP Act was flawed *ab initio* to the extent that the Special Prosecutor (SP) is nominated by the AG and appointed by the President, the SP needs the approval of the AG to initiate prosecutions and the OSP is funded by the Executive. It is no wonder that the OSP, which has been occupied by two SPs so far, has been rendered toothless. If the OSP is to be successful in fighting corruption, it would be important to re-enact its Act and remove it completely from the influence of the Executive, in terms of appointment, prosecution of cases and funding.

<u>"Galamsay":</u>

"Galamsay" is a menace that is wreaking havoc on the country in terms of degradation of our forests and waterbodies—indeed, representing an existential threat for us! Therefore, for the President not to mention it in his SONA was a bit perplexing. The Government has implemented a number of strategies and invested quite an amount of capital in dealing with "galamsay." However, limited success has been achieved so far. This appears to be due to existence of strong vested interests in the business, involving well-placed individuals and groups. It would take concerted efforts in regulation, community engagement and a strong sanctions regime to bring the menace under control and avoid its potentially-disastrous consequences.

<u>II: MPC STATEMENT</u>

<u>Macroeconomic and Financial Developments</u>

<u>Economic Growth</u>:

The Governor reported that growth in 2023 was above expectations. He referred to GDP data released by the Ghana Statistical Service (GSS) that indicated real GDP growth was higher for 2023 compared with the revised target, driven by the services and agriculture sectors. It is a fact, however, that growth in 2023 was still lower than those in 2021 and 2022, implying that the economy is still yet to recover from its recent subdued growth and general crisis, let alone turn the corner as is being suggested by the economic managers.

<u>Inflation:</u>

The Governor stated that inflation had remained broadly stable since December 2023. The February headline inflation had higher food inflation than non-food inflation. This confirms the important role of food inflation in recent inflation trends, a role that needs to be recognised and taken into consideration if inflation is to be controlled on a durable basis. The fact that food accounts for nearly 44% of the CPI basket means that you cannot ignore it when you want to bring inflation under control.

Fiscal Performance:

The Governor stated that fiscal performance was satisfactory in 2023, with a lower deficit than was targeted. The lower deficit reflected almost entirely lower expenditure. Both the lower expenditure and deficit occurred on the back of reduced interest payments due to the DDEP, which was not fully captured in setting the fiscal targets. The fiscal figures must also be considered in the context of suspended external debt payments since 2021, which would make the figures look ordinarily more favourable. Achieving durable favourable fiscal outcomes would require both revenue and expenditure reforms that limit the fiscal gap and the required financing.

Monetary Aggregates:

The Governor reported moderation in year-to-year growth in monetary aggregates—reserve money and broad money—in February 2024 compared with their "explosion" (**my words**) in February 2023. The Governor attributed the moderation to "tight liquidity management efforts." It has to be said, however, that the explosion of these aggregates in February 2023 was fuelled by the excessive monetary financing in 2022, which the BoG and the Ministry of Finance must take blame for. The "tight monetary tightening efforts" the Governor refers to represent the price we have to pay in high interest rates to mop up the huge liquidity injected into the economy through the monetary financing, which also fuelled record inflation and depreciation in 2022.

Credit to the Private Sector:

According to the Governor, Credit to the Private sector by banks "continued to remain weak." He quoted year-to-year private sector credit growth for February to illustrate his point. Credit to the private sector contracted in real terms. In contrast, in February 2024, banks' investments in GOG and BOG instruments rose sharply. These developments reflect massive crowding out of the private sector by fiscal dominance in the economy and misplaced monetary tightening response. The squeeze in private sector credit is having deleterious effect on investment and economic growth. Fiscal retrenchment through expenditure and deficit control is critical to provide needed credit to the private sector to boost investment and growth.

Banking Sector Performance:

The Governor stated that the banking sector's performance had rebounded after the implementation of the DDEP. He mentioned significant increases in banks' assets and deposits. On the other hand, advances (to the private sector) increased only marginally, indicating deprivation of the private sector of much-needed credit that is being gobbled up almost exclusively by Government. The Governor reported that Capital Adequacy Ratio (CAR), liquidity and profitability ratios all improved compared to a year earlier. However, the nonperforming loan ratio increased, said to reflect the downgrading of several large exposures to the banks. It has to be said that, avoiding Government's crowding out of the private sector by closing the deficit gap is critical to reviving the economy.

The Balance-of-Payments:

According to the Governor, Ghana's trade account recorded a higher surplus in 2023 than in 2022, while the current account recorded a surplus in 2023 compared to a deficit in 2022. Significantly, a sharp reduction in interest payment, due to what the Governor described as the "Debt Standstill," contributed to this better outcome. The capital and financial account balance also improved, helped by lower debt amortisation as a result of the Debt Standstill. All put together, the overall Balance-of-Payments (BoP) recorded a small surplus compared with a higher deficit in 2022. As a consequence, BoG's Gross International Reserves (GIR) increased slightly to US$5.91 billion, equivalent to 2.7 months of import cover. This level of reserves, which even includes "pledged assets and encumbered petroleum funds," is grossly inadequate and renders the economy vulnerable to shocks and to speculative attacks on our currency. An update by the Governor indicated that the GIR increased further to US$6.2 billion at the end of February 224, enough to cover 2.8 months of imports. The level of reserves needs to be bolstered through an aggressive export promotion programme.

Exchange Rates:

The Governor admitted that the foreign exchange market came under some pressures—both seasonal and non-seasonal—in February and early March. He reported that in the year to 20th March, 2024, the Ghana cedi recorded a depreciation of 6.8 percent against the US dollar. He, however, stated that the cedi "continues to recover its value." But the question is by what measure? Certainly, not in nominal terms because since he spoke on 25th March, the cedi has continued to depreciate, reaching nearly GHS13 to the dollar. Let us repeat right here that relying on funds from the IMF, World Bank, Eurobonds, cocoa syndicated loan, etc. to bolster the cedi, as we have been doing, is not only "a lazy man's approach," to say the least, but also clearly unsustainable as the pressure would be back on when the loans fall due for repayment. The way to stabilise the cedi on a durable basis is to increase our FX earnings through greater ownership of, and value addition to, our natural resources, to reduce our import demand through domestic industrialisation and to entrench fiscal and monetary discipline.

Policy Rate Decision

In arriving at the MPC Policy Rate decision, the Governor noted the sharp deceleration in inflation in 2023. However, the pace of disinflation had slowed in the first two months of 2024. The BoG's latest inflation forecast suggested a slightly elevated profile. Meanwhile, the BoG saw overall risk to inflation to be slightly on the upside. It was based on the foregoing considerations that the MPC decided to maintain the Policy Rate (PR) at 29.0%. To us, however, the decision is problematic—and difficult to uphold. The MPC's suggested drivers of future inflation are all supply and cost factors. With the PR pegged so high for a year, while inflation has more than halved, monetary policy has been quite tight. Therefore, the decision to maintain the stance when the drivers of inflation are not directly amenable to the PR is puzzling. We have long pointed to futility of using the PR, a demand instrument, exclusively to fight inflation that has strong supply/cost undercurrents. What is needed are complementary measures to address the inflation drivers—food prices, fuel prices, utility prices, transport fares and the exchange—directly. As we have repeatedly argued, interest rates in the country are prohibitively high and represent a drag on investment and growth; and this is because they are being artificially held up by a misplaced and misdirected monetary policy, which has to change!

It has to be pointed out that monetary policy is carrying an unnecessarily heavy burden in respect of macroeconomic adjustment because of pervasive fiscal dominance in the economy. It is important for fiscal policy to bear part of the macroeconomic adjustment by containing the deficit and associated financing. The BoG has also not helped itself by heavily monetising the deficit recently that fuelled demand and inflation pressures, which have necessitated its maintenance of very destructive Policy Rates. Indeed, there is evidence of inadequate coordination between fiscal and monetary policies, which is doing more harm than good to the economy, including in the form of high interest rates, high inflation, persistent currency depreciation and stunted growth. We cannot stress enough the need for coordinated fiscal and monetary policies to promote durable macroeconomic stability and sustained growth.

For further information, kindly write to Dr. John Kwakye, Director of Research, IEA Ghana via email: ***j_kwakye@yahoo.com***