

**GHANA ECONOMIC REVIEW AND OUTLOOK 2003:  
THE STATE OF THE GHANAIAN ECONOMY  
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**1. REVIEW OF YEAR 2002**

This is an opportunity for engagement and dialogue to reach agreement/consensus on “mid-year” policy corrections if any, as well as to begin looking at policy options for next year – an election year.

Ghana’s program with the IMF, which expired on November 30 2002, was originally a three-year Enhanced Structural Adjustment Facility (ESAF) Arrangement for the period May 3, 1999 to May 2, 2002. It was approved for SDR 155 million (about US\$193 million). In November 1999, the ESAF – the then IMF facility for low-income countries – was renamed the Poverty Reduction and Growth Facility (PRGF). Based on a preliminary assessment of Ghana’s eligibility for relief under the Enhanced HIPC Initiative, the IMF decided that Ghana was eligible for assistance under the Initiative and the ESAF Arrangement was converted to a PRGF Arrangement in the original amount of US\$ 193 million. This was increased twice each by about US\$46 million to a total of US\$285 million.

The medium-term strategy set out in 1999 had envisaged:

- Annual real GDP growth of 6 per cent;
- Gross international reserves reaching 3 months of imports cover;
- Domestic debt maintained at or below 20% GDP; and
- A divestiture program that included Tema Oil Refinery, Ghana Airways, Ghana Railways and the Electricity Corporation of Ghana.

None of these was realized when the Arrangement expired on November 30, 2002. Real GDP growth for 2002 of 4.5 per cent was 33 per cent short of the 6 per cent target; gross international reserves were the equivalent of only 1.9 months import cover compared to the 3 months target; and the domestic debt stock had risen sharply – to almost 29% GDP.

Looking back over the life of the Arrangement the IMF staff concluded rather wistfully: “The sustained improvements in Ghana’s economic performance that had been hoped for were

undermined by recurrent policy weaknesses.... In the event, erratic fiscal and monetary policies and persistent delays in structural reforms have left the economy little stronger (and in some respects, such as the domestic debt burden, weaker), than it was four years ago...The 4.5 per cent real GDP growth and the 15.2 per cent (year-end) CPI inflation figures for 2002 compare with 4.7 per cent real GDP growth and 15.8 per cent inflation recorded in 1998”.

## **Public Finance**

The medium-term macroeconomic strategy is an integral part of the Ghana Poverty Reduction Strategy (GPRS) intended to take the economy out of the trap of rising debt and escalating inflation. Consequently, the fiscal program for 2002 aimed at reallocating expenditure towards social objectives, while substantially reducing domestic arrears and keeping the stock of domestic debt on a clear downward path.

New revenue measures—with annualized yield of 1.9% GDP—aimed to place government finances over the medium-term on a sustainable footing. A key element was an increase in the VAT rate by 2.5 percentage points. This had an expected yield in 2002 equivalent to 0.7% GDP. Implementation was left for mid-year arguably to make for more time “to build consensus and create the requisite positive political environment”. This may have been deemed necessary because of the turbulent history of the VAT in Ghana.

Steps were also taken to strengthen revenue collection and administration including the creation of a National Tax Audit Team and the appointment of head of the Revenue Agencies Governing Board (RAGB). The RAGB was tasked, among other things, to ensure full implementation by CEPS and IRS of the common Taxpayer Identification Number (TIN) system.

The effective control and monitoring of public expenditure was of utmost importance to successful implementation of the 2002 fiscal programme. The establishment of effective expenditure control, particularly at the commitment stage was considered “a central plank of the program and a prerequisite for ensuring the appropriate use of interim debt relief under the Enhanced HIPC Initiative”.

The attempt to contain total spending in the face of revenue shortfalls and expenditure overruns led to the compression of capital spending and a build-up of arrears to the DACF, GETF, SSNIT,

contrary to the stated objectives above. The failure to control the wage bill sufficiently was seen (by the Bretton Woods Institutions and the donors) as indicative of continuing problems with expenditure management, “the improvement of which was a key objective under the program”. Ad hoc measures to restrain cash expenditures, however, can be counterproductive.

According to the Ministry of Finance, the factors that contributed to the wage bill overrun were:

- Unbudgeted wage increases to staff in the Ministries of Health and Education, in part to stem mass exodus of staff and service disruptions;
- MDAs, particularly, some subvented organizations, did not universally apply the established procedures for controlling wage and salary expenditures (emphasis added); and
- Unbudgeted increases in allowance mostly to health workers.

The lessons from the recent past are clear. The principal one is that little can be achieved without realistic budgeting and fiscal discipline. The commitments that are finally approved by Parliament should be consistent with the most realistic projections of revenues and financing resources, including divestiture proceeds. Where flows are volatile, clear contingency plans should be spelt out. Ad hoc schemes that set lower ceilings than implied in the Budget approved by Parliament and moreover, originating from the Ministry of Finance which made the revenue projections in the first instance are not particularly useful. If the Ministry of Finance enforces the cash restraints, they result in payment arrears. And where the cash restraints prove unenforceable (as in election years) they most likely would result in excessive net domestic financing and rising domestic debts.

### **Money and Banking**

The year 2002 clearly demonstrated that a ‘business as usual’ attitude to policy-making could never transform the Ghanaian economy. Believing, and taking credit for the decline in the rate of inflation from the first quarter of 2001, the Government aimed for a single digit rate of inflation by the end of 2002. As with the Government of the National Democratic Congress (NDC) in 1998, the Government of the New Patriotic Party (NPP) ignored CEPA’s warning that the inflationary trend appears to be just following a three-year cycle of troughs and peaks, and that a more radical policy may be needed to change that trend. Such a radical change in the policy regime would have to depend on a detailed analysis of the causes of inflation in Ghana. Whatever, the causes of inflation, it is clear that we cannot rely on monetary policy only to hold

inflation at bay. Avoidance of fiscal excesses and active policies to revamp the real sector are credible complements. Without a change in policy and full cooperation from the fiscal authorities, monetary policy will remain just a passive appendage to the economic policy making process in Ghana, lending itself to accommodation of fiscal excesses.

The process of recreating the central bank as an active and independent policy-making body was accelerated in 2002. First was the passing of the new Bank of Ghana Act (Act 612) that sought to assert the independence of the central bank. While the new act confers *de jure* independence on the central bank, the real test of such independence is in the central bank's operations. In a developing country like Ghana, which faces chronic structural deficits, monetary accommodation becomes more or less a social obligation on the central bank.

Clearly, the high growth of monetary aggregate in the last quarter can be directly linked to the financing of cocoa purchases. In the first place, the borrowing of the \$420 million dollars to finance the purchases swelled-up the Net Foreign Assets (NFA) by about 51 percent and 132 percent in the third and fourth quarters, respectively. The contra on the uses side is the increases in both Currency in circulation and Demand Deposits for the last two quarters of the year. Currency in circulation increased by 50 percent while Demand Deposits increased by a whopping 74 percent: the result was almost 60 percent increase in Narrow Money. The inflationary consequences of such high injection of liquidity are quite predictable.

Inflation has continued to be as elusive as ever. Having peaked in March 2001, it set itself on its traditional 18-month downward path towards a trough in September 2002. Despite repeated cautions by CEPA the NPP Government, just like its predecessor, took credit for the decline in the rate of inflation. By October 2002, the year-on-year rate of inflation had begun its 18-month predictable ascent, which without proper intervention will reach its peak in the first quarter of 2004.

A discomfiting observation is the fact that the country has still not been able to stabilize food prices throughout the year. Surprisingly, the second half of the year, which coincides with the harvest season, registered higher food inflation than the first half. A possible explanation is that for the off-harvest season there was a lot cheaper food imports to supplement domestic production.

Low inflation benefits the poor – their wages and cash assets retain more value. But policies to reduce inflation – tight fiscal and monetary policies – could adversely affect the poor through, for example, reduced availability of public services such as health and education. A rise in interest rates – aimed at reducing inflation – could impact negatively by making credit more expensive and reducing economic activity. The key policy question is by how much and how quickly should inflation be reduced?

The banks continued to reap huge profits by taking advantage of an imperfect market situation characterized by a government with an insatiable appetite for loanable funds and a lukewarm banking public. Large investments in high-yielding Government bills, high rates on advances to businesses, low interest rates on deposits, and charges and levies on the banking public are the ingredients of this lop-sided market situation in which an implicit collusive behaviour is holding other stakeholders captive.

Although the number of banks in Ghana has increased in recent years and new services have been introduced, the money market exhibits a kind of inflexibility suggesting an oligopolistic structure. Instead of the increased number of banks generating competition leading to reduction in cost of bank-service provision to customers, there has been a race for higher profits by most banks.

As if the high interest rates were not enough, bank customers are levied charges and commissions of all sorts. A customer making deposit is first cautioned about a ‘minimum deposit’. If the deposit falls below such specified minimum, the customer is levied a charge. In some banks, the minimum deposit can be as high as one million cedis – clearly out of reach of the average Ghanaian. Other levies, which are difficult to explain or justify, include so-called periodic charges on accounts even when they have been dormant. This is as in ancient times when the major role of banks was safekeeping of valuable assets. It is only under such an archaic idea of banks rendering safekeeping services that these periodic charges on dormant accounts can be justified; but certainly in modern day banking the practice is untenable.

## **Trade and Payments**

The real exchange rate – the nominal rate adjusted for inflation - which had appreciated in 2001, depreciated moderately in 2002, resulting in the continued overshooting of the exchange rate. The cedi appears to be undervalued by 30 percent and the gap between the actual exchange rate and the PPP rate has widened. As reported in last years' CEPA's *Macroeconomic Review and Outlook*, some countries in the early phases of the transition to accelerated growth have used an undervalued real exchange rate to provide a stimulus to exporting. In Ghana, it does not appear to be a deliberate policy to maintain an undervalued currency as an incentive to exports. Rather, there is a political preference for a stronger currency. Part of the overshooting is coming from the sticky prices in the water, electricity, telephones, and the petroleum and transport sectors of the economy. Prices in these sectors are controlled by public agencies and are not allowed to adjust to their scarcity levels. Since 1999, changing these prices has been problematic.

The improvement in the balance of payments was trade-led: the good performance on the trade account partially compensated for the poor performance on services and the unexpected disappointment on the capital account. The trade performance was triggered by the favorable developments in the external terms of trade, largely in the second half of the year, on account of increases in the world market prices of Ghana's major exports and a stable crude oil price.

Both cocoa and gold prices increased significantly in the course of year 2002. Cocoa prices in the world market rose by 64 percent partly as a result of the political crisis in La Cote d'Ivoire generating negative expectations about world cocoa supply. Gold prices on world bullion markets on the other hand increased by 15 percent in the course of the year.

While exports increased, imports decreased by 8.8 percent in value between 2001 and 2002. Most of the decrease occurred in non-oil imports, which declined from US\$2,451.7 million in 2001 to US\$2,197.0 million in 2002. Oil imports declined by less than 2 percent as the price increased by about 2 percent.

The combination of increasing exports and decreasing imports led to a 40 percent decline in the trade deficit from US\$1,101.4 million in 2001 to US\$641.2 million in 2002. This represents the lowest trade deficit in the last five years. The improved trade performance was partially offset

by a weak services performance. The deficit on Services increased from US\$182.1 million in 2001 to US\$243.4 million in 2002.

The capital account recorded a net outflow of US\$47 million. This may be the first time since the effective implementation of the economic reform programme in 1984. The data, however, needs careful interpretation. Under HIPC most of the assistance is increasingly in the form of debt relief. This means that presentationally, the capital account of the Bank of Ghana would record amortization due (inclusive of the debt relief component – roughly 55 per cent of total). The debt relief is treated as a financing item.

Ghana's external debt stock increased by 12.3 percent from US\$6,208 million at the end of 2001 to US\$6,973 million at the end of 2002. The increase was largely on account of huge borrowings from bilateral sources, increased use of IMF standby SAF/ESAF and extended fund facilities, and increased level of the short-term suppliers' credits in respect of crude oil and cocoa purchases.

### **Agricultural Sector**

Overall agricultural production in 2002 was reportedly better than ever, according to our survey of farmers and Ministry of Food and Agriculture officials in all ten regions of Ghana. Farmers, MOFA officials and NGOs interviewed indicated that agricultural yields in 2002 increased over the levels in 2001. All crops – food, cash and tree crops – experienced the increases in output.

The overall increase in production, according to farmers, could be attributed to the favorable rainfall pattern, prompt and early planting, disease control and better management of weeds. MOFA officials, on the other hand, attributed the increase to favorable rainfall pattern, increased acreage, and extensive use of improved seeds.

Attempts at introducing improved technologies have had limited impact. The level of mechanization of agriculture is rudimentary and inadequate water management systems limit the effective farming season, resulting in complete dependence on nature. Ghana needs an improved agricultural technology that can be adopted by small-scale farmers or an institutional framework that allows small-scale farmers access to improved technology on a sustainable basis for a sustainable increase in agricultural productivity.

## 2. GENERAL OUTLOOK (2003)

### Background

The nation's fundamental goal is to achieve "sustainable improvement" in the living standards of Ghanaians through faster economic growth, employment generation and a reduction in poverty.

According to the IMF: To ensure that its resources are used effectively to promote (agreed goals), the IMF lends to support policies that are likely to further those goals. Disbursements under IMF loans are therefore conditional on satisfactory implementation of the policy program. Moreover, the BWIs "play a special role within the aid community vis à vis the government.

An important lesson from the recent past is that aid flows may not only be volatile; they are also prone to be procyclical. Donor conditionality could lead to good performance being "rewarded" - with disbursements in the amounts agreed and as scheduled over time - and poor performance "punished" - with less than programmed flows and/or delays.

Thus in 2002, among others:

- the World Bank failed to disburse some US\$27 million on account of GCB divestiture conditionality not being met;
- the US\$54 million financing gap which donors agreed at the April Consultative Group Meeting held in Accra was not disbursed;
- the final disbursement of some US\$ 66 million under the PRGF Arrangement with the IMF was not disbursed because the fifth Review could not be completed; and
- agreements reached with the Paris Club creditors (under the HIPC Initiative) apparently lapsed at end-November, resulting in Ghana receiving debt relief in the amount of over US\$100 million, less than had been programmed.

In this context, the structural conditionalities in respect of GCB divestiture, the financial health of state-owned enterprises such as Tema Oil Refinery (TOR), Volta River Authority (VRA), Electricity Corporation of Ghana (ECG) and Ghana Water Company Limited (GWCL) requiring automatic price adjustment of their products and the difficulties with their implementation send worrisome signals on the Poverty Reduction and Growth Facility (PRGF) agreed in May 2003.

## **Fiscal Outlook**

The overall outlook for 2003 would depend on achieving a fiscal performance consistent with the following:

- zero net domestic financing (NDF) of fiscal operations to ensure complementarities with monetary policy objectives;
- no accumulation of new payment arrears;
- significant increases in capital expenditure in support of the poverty-related triggers (noting the desirability of reaching Completion Point as early as possible next year);
- no quasi-fiscal losses at TOR or the public Utilities - conditionalities in respect of Ghana Commercial Bank divestiture were, in part, to ensure this.

The quest for this requires among others:

- Sound economic policies, developed and “owned” by the country, and consistently applied over time;
- Stronger domestic institutions, both public and private; and
- Financial resources.

Delivering on this agenda would no doubt be a formidable task.

On the revenue front the National Health Premium (NHP) – second-best choice even with all the provisions that make it all but in name a VAT rate increase – requires careful marketing. There is need to clarify the role of SSNIT and implications of requiring contributions from all except the aged. The delay in getting the law passed for implementation to commence is bound to create financing problems for the current Budget.

The debt recovery levy (DRL) on the Tema Oil Refinery debt bonds is also threatened by:

- world market price developments (petroleum prices have not followed the projected downward trend);
- the ad valorem excise duty raises the ex-pump price beyond the increases in the ex-refinery price; and
- malfunctioning of cross-product price subsidy policy.

On the expenditure side, the pre-conditions for flexibility are not sufficiently evident. To give managers the needed room to manoeuvre, key requirements include:

- authority to make reallocation across line items; and
- a medium-term framework.

The reality is that a substantial part of the government expenditures is non-discretionary, and this includes the wage bill. Neither the number of employees nor the wage/allowance structure is under the control of the management of the MDAs. Indeed, as noted by the IMF, public officials accused (see above on the wage bill overrun) of failure to apply established rules complained of lack of political mandate to enforce the very rules.

In view of the cost escalations following upon the Jan 17 petroleum products price hikes, upward adjustments were made in the nominal allocations for GPRS-defined poverty related expenditures.

Traditionally the first quarter expenditures reflect non-discretionary spending and payment carryovers from the preceding year. When interpreting first half year performance in relation to expenditures and payments, all these, as it were, seasonal factors, must be fully taken into account. Wasteful and inefficient spending must not be countenanced, but payment arrears and quasi-fiscal losses are illusionary and not sustainable. Payment arrears to the private sector lock up working capital and unfunded losses of SOEs arising from public policy directives simply add to the domestic debt currently standing at 29% GDP.

### **Money, Credit and Inflation Outlook**

2002 ended with a failure to achieve most of the monetary targets that were set. Both inflation and monetary targets were tripped. While monetary accommodation of fiscal excesses was partly to blame, the inability of the monetary authorities to effectively sterilize foreign inflows accounted for the weaknesses experienced in the last quarter. Economic outturn for 2003 and beyond will hinge on the ability of the monetary authorities to withstand fiscal pressures and to sterilize external inflows.

In the 2003 Budget Statement, the overall monetary objective was to reduce the rate of inflation and exchange rate volatility while pursuing policies to ensure adequate bank credit was available to support growth of the real sector.

Following the 94% hike in petroleum prices and the subsequent jump in inflation from 15.2% in Dec. 2002 to 29.4% in Feb. 2003, the inflation target of 9% by end year was revised upwards to 22%. On current trends, even this revised target could prove optimistic.

The February binge in inflation ‘disturbed’ the familiar three-year cycle of Ghana’s inflationary trend. Without the February price level shock inflation would have been on a gentle upward trend till it peaks in February/March 2004. This means that *ceteris paribus* 2004 would have seen inflation on a downward trend. Consequently, if the current efforts of both the monetary and fiscal authorities at containing inflation is maintained and barring any further price level shocks, Ghana could see a single digit inflation by end of 2004.

### **External Sector Outlook**

Barring any unforeseen developments in the capital accounts of the balance of payments, Ghana can expect another trade-led balance of payments improvement in 2003. This may be accompanied by a real exchange rate appreciation if tight monetary policy is maintained.

Continuing uncertainty in the supply of cocoa from the political instability in La Cote d’Ivoire may subject cocoa markets to some instability. Part of the price gains last year may be reversed. However, these prices are unlikely to be completely reversed, implying that coca prices may remain relatively high though lower than the average for 2002. On the supply side, the volume of cocoa exports can be expected to increase partly as a result of the three years of mass spraying and increased real producer prices, and partly as a result of diversion from La Cote d’Ivoire.

Gold prices have remained high over the last two years. They are unlikely to drop in the face of continuing uncertainty about world economic recovery.

On the imports side, the huge upward adjustment in the domestic prices of petroleum products combined with stagnant real per capita incomes will reduce the volume of crude oil imports. The declining trend projected for world market prices of petroleum (and products) after the Iraq war

has unfortunately not been realized. The implications for our oil bill and for TOR/consumers are naturally issues of considerable public concern.

### **Agricultural Outlook**

Overall, there was optimism regarding the sector’s performance for the year. Improved yields are anticipated for the 2003 agricultural cycle given the early rains at the beginning of the year.

The regional and district officers of the Ministry of Food and Agriculture as well as the agriculture officers of the NGOs interviewed were asked to provide an assessment of agriculture performance for 2003 on the basis of the mini-harvest and the rainfall pattern. Rainfall was chosen as an indicator of agricultural performance because of the almost total reliance of farmers on rain.

On the basis of the mini-harvest, the Ministry of Food and Agriculture staff tended to be more optimistic than the agriculture officers of NGOs and more willing to make a forecast. On the basis of the rainfall patterns the NGO officials were just as optimistic as was the staff of the Ministry of Food and Agriculture.

### **3. FIRST HALF-YEAR DEVELOPMENTS**

Any serious review of the details of projections and performance must take full account of economic trends and their possible implications.

**Table 1: Overall Expenditure Performance January – May 2003**

	<b>Projected</b>	<b>Provisional</b>	<b>“Savings” %</b>
<b>Recurrent</b>	5168	3918	24
<b>Capital</b>	2251	1402	38
<b>Total</b>	7419	5320	28

Source: Bank of Ghana Statistical Release, Fiscal Developments Vol. 1, November 4, 2003

Leaving aside HIPC financed expenditures, total payments amounted to ₵5320 billion compared to projected expenditures of ₵7419 billion for the 5 month period. This implies an overall “savings” of ₵2099 billion representing nearly a third of planned spending. Past experience and the nature of the budget approval process would caution that these “savings” may be indicative

of serious net accumulation of payment arrears which could serve as dampening pressure on the tempo of economic activity at least in the modern sector.

**Table 2: Recurrent Expenditure**

	<b>Projected</b>	<b>Provisional</b>	<b>“Savings” %</b>
<b>Non-Debt</b>	3475	2766	20
<b>Interest (Debt)</b>	1692	1152	32
Domestic	1333	898	33
External	359	254	29
<b>Recurrent (Total)</b>	5168	3918	24

Table 2 provides a breakdown of the savings – 24% of planned expenditures – in respect of recurrent expenditure. Non-debt payments were a fifth less than projected while interest payments were a third lower.

Both components – domestic and external – of interest payments recorded savings. Domestic interest payments were about a third lower than projected. Over the period under review, the Bank of Ghana (BOG) prime rate was raised in two installments by a total of 3 percentage points and interest rates on Treasury bills followed in the upward direction. Consequently, the apparent savings on interest account calls for some explanation for the implications to be better appreciated.

The “savings” in respect of external interest payments could be simply a matter of presentation. There is reason – from past experience – to believe that while the projected payments shown in the table may be referring to what was due to be paid, the provisional actuals may be what was actually paid. In this case, however, the difference need not indicate payment arrears. It may represent portions of the debt relief to be paid into the HIPC Account set up at the Bank of Ghana. External payment arrears are forbidden by a conditionality under the PRGF Arrangement with the IMF.

**Table 3: Non-Debt Expenditures**

	<b>Projected</b>	<b>Provisional</b>	<b>Savings %</b>
<b>Personal Emoluments</b>	2271	2014	11
<b>Good and Services</b>	829	392	53
<b>Transfers</b>	376	361	4
<b>Total Non-Debt</b>	3475	2766	20

As seen in the table, again all components of non-debt spending contributed to the recorded savings of 20% on non-debt expenditures.

Personal emoluments or the government wage bill represent as the name implies the wages and salaries of employees in the public sector – the Civil Service, Security Agencies and subvented organizations. Against the background of the protracted wage negotiations and reports of ongoing discussions over terms and conditions of service and payments in the education sector in excess of provisions, it is difficult to see this component of savings as other than payment arrears. The evidence suggests strongly that some categories of public sector employees failed to receive their full remuneration during the period under review.

The most disturbing development, however, is the recorded savings in respect of goods and services. The table shows that payments actually made over the period were less than half what had been budgeted for. This category includes various goods including electricity, water, office supplies, maintenance and repairs as well as allowances to government employees. Again, without further explanation, it is hard not to conclude that all or a substantial part of this must be simply payment arrears.

Transfers to various funds including SSNIT, the GETFund and petroleum-related fund also produced savings equivalent to 4% of the planned. The available information is not detailed enough to determine which of these funds have been affected. The controversies about past arrears in relation to the GETFund call for more light to be shed on the nature of these savings.

**Table 4: Capital Expenditure**

	<b>Projected</b>	<b>Provisional</b>	<b>Savings %</b>
<b>Capital Expenditure (domestic)</b>	1113	828	26
<b>Capital Expenditure (foreign)</b>	1138	573	50
<b>Total</b>	2251	1402	38

As with all the other components of expenditure, payments in respect of capital spending – the development budget – also registered savings. Domestic capital expenditures are those funded from our own resources. Here payments fell short of the planned by about a quarter. Included in this category are transfers into the District Assemblies Common Fund (DACF). As revealed in the Budget Statement (2003), the stock of payment arrears had already reached a level where

clearance would have to be spread over five years. It is important that the reported savings are not indicative of further growth of the stock of arrears.

Payments in respect of foreign-financed capital expenditures also show a “savings” of 50%. This means spending over the review period amounted to only one half of what had been planned. As would be evident from the examination of revenue performance, aid flows this year have once more proved volatile and unreliable.

Foreign-financed capital expenditures are funded with project loans and project grants disbursed to the Budget. In the period under review, receipts of project grants amounted to just about 40% of expected i.e. less than half of the projected receipts had actually arrived. Information on project loans is not readily available but could not, on the evidence, be much better.

## **Revenues**

There is no doubt whatsoever that the revenue collecting agencies have intensified their efforts. Indeed this is a critical assumption that underpins the analysis to follow. The steps taken to improve collection include the following.

- i. An electronic clearing system has been introduced this year “to enhance collection in addition to the distress action adopted as a way of enforcing the law of default in the payment of excise duties”.
- ii. The Internal Revenue Service (IRS) is embarking on an exercise to identify elusive night operators like “the fried rice and jollof sellers known commonly as ‘check check’”.
- iii. The change of the method of revenue collection from daily payment to the use of stickers in the transport sector has contributed enormously towards the receipts from that area.
- iv. “Hitherto, the receipts from airport taxes were allegedly used by the collectors and refunded later, and the practice has been stopped”.
- v. “Furthermore, the installation of GCNET, a computer mechanism to assess duties to be paid at various ports of entry, is all designed to enhance the country’s revenue mobilization”. (Graphic September 3, 2003).

**Table 5: Total Revenue and Grants**

	<b>Projected</b>	<b>Provisional</b>	<b>Difference % (+ excess) (- shortfall)</b>
<b>Total Revenue</b>	4620	4702	2
<b>Grants</b>	1421	994	-30
Project	507	206	-59
Program	678	226	-67
HIPC (multilateral)	236	561	138
<b>Total</b>	6041	5696	-6

Receipts of revenues and grants fell short of expenditure by 6%. This was on account of poor performance of traditional grants – project and program. Debt relief provided by the multilateral agencies – IMF, World Bank and the African Development Bank – in contrast was more than double the projected. The total projected for the year of ₪235.5 billion compares to disbursements up to May of ₪561 billion suggesting that disbursements of HIPC assistance from the multilateral agencies may have been faster than anticipated.

Total revenue showed a marginally better than anticipated performance with an excess total collection of 2%.

**Table 6: Total Revenue**

	<b>Projections</b>	<b>Provisions</b>	<b>Differences</b>
Tax	4196	4573	9
Non-Tax	168	129	-23
New Revenues Measures	256	0	-100
<b>Total</b>	4620	4702	2

Table 6 provides the breakdown of total revenues into tax, non-tax and new measures. As of end May, none of the new measures had recorded any results. This could be due to delays in legislation and implementation as, for example with the National Health premium. The other key new measure – the debt recovery levy (DRL) of ₪640 per unit of sale of petroleum products – may also have run in problems because the landed price – cedi value of import parity – has remained stubbornly higher than projected. After the higher than expected jump in the CPI-based inflation after the January 17 petroleum-product price hikes, it is understandable why Government may find further price increases intolerable.

The implication, however, is that the automatic petroleum product price adjustment mechanism agreed with the IMF – a conditionality under the current PRGF Arrangement – has been in effect suspended. Unless there is a sharp fall in the world market price for petroleum, the target of yield from this levy for the year is not realizable.

Non-tax revenues also fell short of projected by 23%. Details are not available to enable a meaningful appraisal and the implications of this development for the rest of the year.

**Table 7: Tax Revenue**

	<b>Projected</b>	<b>Provisional</b>	<b>Difference %</b>
<b>Direct</b>	1240	1391	12
<b>Indirect</b>	2061	2179	6
<b>International Trade</b>	896	1003	12
<b>Total</b>	4197	4573	9

The excess of collection of total tax revenue over the target of 9% resulted from over-performance in every component – direct, indirect and international trade. Direct and international trade taxes each recorded an over-performance of 12% above the set target. Indirect tax collections also over-performed but by a more modest 6%.

**Table 8: Direct Taxes**

	<b>Programmed</b>	<b>Provisional</b>	<b>Difference %</b>
<b>Companies</b>	523	463	-11
<b>Other Direct</b>	717	929	30
<b>Total</b>	1240	1391	12

Over the period under review, receipts of company taxes fell short of the target set under the programme by about 10 per cent. Other direct taxes comprising PAYE, Self-employed, Rent income and others, however, together recorded excess collections of about a third.

The Daily Graphic of September 2, 2003 reported that according to Mr. Harry Owusu, Executive Secretary of the Revenue Agencies Governing Board, Pay As You Earn (PAYE) registered “a shortfall of 2.71 per cent” while Self Employed yielded “¢114.92 billion against a target of ¢145.73 billion. The shortfall of ¢30.81 billion is equivalent to 21%. His figures also confirmed the fact of shortfalls in company tax collections.

**Table 9: Indirect Taxes**

	<b>Projections</b>	<b>Provisional</b>	<b>Difference%</b>
<b>VAT</b>	1138	1280	12
<b>Domestic</b>	437	368	(16)
<b>Imports</b>	702	912	30
<b>Petroleum</b>	737	721	(2)
<b>Other Indirect (Excise)</b>	186	178	(4)
<b>Total</b>	2061	2179	6

As shown in Table 7, total collections of indirect tax over the period under review was 6% higher than the target set. Table 9 presents a breakdown by the major categories – VAT both domestic on goods and transactions as well as on imports, Petroleum (taxes and levies) and Other Indirect taxes (mainly excise duties).

VAT collections, overall, recorded a 12% excess over the set target. This was on account of import VAT which was almost a third higher than its target. Domestic VAT collections in contrast showed a 16% shortfall.

The collections of taxes and levies on petroleum products – an ad valorem tax, specific excise, Road Fund levy, etc. put together registered a 2% shortfall. After the sharp price increases announced on January 17, 2003 it would be normal to expect reduced consumption. Moreover, not enough detailed information is available to determine how the products have been affected. The only conclusion that can be drawn is that consumption of petroleum products, over the period under review, was lower than should have been anticipated.

Other Indirect Taxes (excise duties) also recorded lower collections – about 5 per cent – than had been expected. Given the increased collection effort of the revenue agencies, this would again suggest that the tax base – excisable goods – grew at a slower pace than had been anticipated.

**Table 10: International Trade Taxes**

	<b>Projected</b>	<b>Provisional</b>	<b>Difference %</b>
<b>Import Duties</b>	804	912	13
<b>Export Duty</b>	92	91	(0)
<b>Total</b>	896	1003	12

Collections of taxes on international trade were dominated by import duties with export duty being just short of target. The cedi appreciated in real terms on the forex market i.e. domestic costs increased faster than the rate at which the cedi lost value, for example, against say the US dollar by an amount in excess of inflation in the USA.

When the exchange rate appreciates in real terms – lags behind market equilibrium levels - exports tend to contract and imports increase. To correct this situation, a devaluation is almost always necessary – to encourage exports (making exporting profitable) and discourage imports (making these more expensive). The benefits depend on who produces for export or i.e. competition with imports (food farmers) and who consume imports. If a devaluation would hurt the poor, its benefits should be weighed against the cost of continued trade imbalances. The key policy question then is the extent and pace of currency devaluation.

**Table 11: Banking System Credit to Private Sector**

	<i>Credit to Private Sector (CPS) (¢ billion)</i>		<i>Nominal CPS Growth Year on Year (%)</i>	<i>CPI Inflation Year on Year (%)</i>	<i>Real CPS Year on Year (%)</i>
	<i>2002</i>	<i>2003</i>			
Jan	4489.6	5930.9	32.1	16.3	13.6
Feb	4615.8	5522.5	19.6	29.4	-7.5
Mar	4773.7	5786.2	21.2	29.9	-6.7
Apr	4866.0	5811.5	19.4	30.0	-8.2
May	5046.7	6176.1	22.4	29.8	-5.7

*The BOG Prime Rate was increased from 24.5% in Dec. 2002 to 25.5% in January 2003 and further to 27.5% in March 2003.*

The BOG prime rate increases and the stepping up of its Open Market Operations (OMO) were clear signals to the banking sector of its determination to tighten monetary policy. At the same time a rise in interest rates with the aim of reducing inflation by making credit more expensive and reducing the pace of economic activity could have a negative impact on employment and poverty.

It is noteworthy from the table that in the month following upon each prime rate increase—February and April—sharp decelerations in the growth of the stock of credit outstanding to the private sector were recorded (19.6% in February and 19.4% in April).

These responses in private sector borrowing from the banking system are in themselves what rational decision-making would lead one to expect. They suggest that the instruments of policy are effective. What raises some concern is the extent of deceleration in the rate of borrowing. The Table shows that the real stock of credit in the period since February this year has been lower and by significantly large margins than the corresponding stocks of last year. It is this observation that adds to evidence from elsewhere of a slower tempo of overall economic activity—measured for example by real GDP growth—at least than projected in the PRGF programme agreed with the IMF.

#### **4. CONCLUSION**

The strong hypothesis that emerges from the survey of performance in the first half year is that the tempo of economic activity – as measured, for example, by the real GDP – has been slower than had been anticipated in the PRGF Arrangement with the IMF for 2003.

- Real appreciation of the exchange rate is consistent with higher imports, higher than projected collections of import duties and import VAT. At the same time, it makes Ghana's exports [agricultural produce, handicrafts and manufactured goods and services (including tourism)] less competitive with adverse consequences for profits, production and employment. Perhaps, even more seriously, the domestic import – competing sector becomes flooded with relatively cheaper imports. The poultry industry has threatened to take its case to court.
- All tax collections on domestic income have fallen short of their targets (company tax, self employed, PAYE, domestic VAT, excise duty and petroleum tax).
- The stock of real credit to the private sector from the banking system in 2003 has been persistently lower than that of 2002. (See Chart 1) although in nominal terms there has been moderate growth (see Chart 2).