

EXECUTIVE SUMMARY

On January 7th 2001, Ghana crossed a critical landmark in her political history. Four years previously, the country saw for the first time since Independence, the completion of the term of office of a Government, elected under a multi-party constitutional regime. On the later occasion, an elected President smoothly handed over the governance of the realm to another from a different political party. The euphoria that greeted this occurrence from Ghanaians at home and abroad and the recognition of the momentous event by the international community yielded a “democracy dividend” amounting to an estimated 10% of GDP – comprising 8.3% GDP of “exceptional financing” support from the international donor community and about 1.7% GDP of private transfers and tourism receipts. This facilitated the macro stabilisation process of calming down inflationary expectations, stabilizing the exchange rate, halving the rate of inflation, sharply reducing the nominal rate of interest (even if the real rate remained uncomfortably high in the context of high enterprise indebtedness to the banking system) whilst at the same time achieving a modest rebuilding of the nation’s international reserves.

Ghana formally opted for the enhanced Highly Indebted Poor Country (HIPC) Initiative of the Bretton Woods Institutions (BWIs) in February 2001, quickened the preparation of the Poverty Reduction Strategy Paper (PRSP) dubbed the Ghana Poverty Reduction Strategy (GPRS) and reached Decision Point on February 7 2002 after two months delay on account of the need to rectify the misreporting of monetary data.

The underlying framework of this *Macroeconomic Review and Outlook (2001)* is that the Government of Ghana is committed to the ‘trilemma’ objective of sustainable macroeconomic stability, economic growth with productive employment generation, and poverty reduction. In any case the path from the HIPC Decision Point — achieved in February 2002 — to the Completion Point is flagged with floating triggers which signal when the requisite progress has been made and for debt relief to become automatic under the Enhanced HIPC Initiative. The presumption of CEPA is that the national interest

would be best served if any temptation to resort to fiscal illusions is firmly resisted and all stakeholders — the government, development partners, and civil society — work together to ensure an early attainment of the Completion Point, preferably before election year 2004.

These considerations are particularly important because the present PRGF Arrangement, first agreed in May 1999, has been extended by a few months to November 2002. The assumption is that, its successor will be based on a hopefully more complete Ghana Poverty Reduction Strategy (GPRS) document and influenced by a thorough analysis of the chequered record of the present one. Several waivers of performance criteria had to be granted and serious instances of misreporting have been noted — some dealt with, others glossed over. The statistical problems have assumed alarming proportions with uncertainties stretching from national income and price (inflation) data to monetary, balance of payments, and debt data (both domestic and foreign).

Then there is the problematic and thorny issue of election year spending excesses. The above considerations and the national interest of attainment of Completion Point before election year 2004 must all be factored into the design of the successor of the current PRGF Arrangement, which will be effective over the next three years. There is legitimate concern that, if only by default, all efforts will be concentrated on macroeconomic stability. Such an outcome would be as unfortunate as it will be unviable. Stagflation — an economic condition characterised by the coexistence of rising prices, high rates of unemployment, and little or no economic growth — is an outcome that cannot be ruled out, albeit being inconsistent with the fundamental goals of poverty reduction and early attainment of Completion Point.

Public Finance and Fiscal Operations

- *Overall Fiscal Performance*

The domestic primary balance (DPB) using the official payments data improved from 2.2 percent of GDP in 2000 to 3.3 percent of GDP in 2001. On commitments basis the DPB improved from a surplus of 0.1 percent of GDP in 2000 to a surplus of 1.1 percent

of GDP in 2001. This improvement was both on account of better domestic revenue performance and an apparent success in containing expenditure commitments.

Compliance with IMF demands, which is reflected in the official reports, had created the illusion of good fiscal health at the price of a rapid build-up of the stock of payments arrears. The provisional outcome suggests that the year 2001 was no different from the past in that respect.

On commitments basis, the broad measure of fiscal performance — the overall broad balance (OBB) — registered a deficit of 9.8 percent of GDP in 2001, an improvement over the 2000 deficit of 10.2 percent of GDP. However, on accrual basis, the OBB recorded a deficit equivalent to 10.4 percent of GDP in 2001, marginally worse than the deficit of 10.3 percent of GDP in 2000 mainly on account of settlements in respect of divestiture-related liabilities such as retrenchment costs and severance pay.

- *Government Fiscal Operations*

In the area of government fiscal operations, net foreign financing — including exceptional financing — improved tremendously from an abysmal negative 0.2 percent of GDP in 2000 (on account of large loan repayments equivalent to 9.2 percent of GDP) to 7.7 percent of GDP in 2001 on account of larger inflows of project loans, lower loan repayments, and a surge in exceptional financing propelled by deferrals of \$228 million of loan repayments due in 2001 agreed with the Paris Club.

Correspondingly, net domestic financing — adjusted for domestic payment arrears — declined from 9.3 percent of GDP in 2000 to 2.3 percent of GDP in 2001. Government domestic borrowing in 2000 exceeded the requirements for non-divestiture financing of the deficit by 2.3 percent as a result of a net outflow of foreign resources in spite of the accumulation of external payments arrears. Domestic borrowing in 2001, however, accounted for only 23.3 percent of the financing needs, mirroring the exceptionally favourable net foreign inflows.

Official domestic financing of the fiscal operations of government — the PSBR reported by the Bank of Ghana— is a key performance criterion of the IMF's Poverty and Growth Facility (PRGF) Arrangement with Ghana. In an effort to meet the ceiling for the PSBR the government has often resorted to hidden liabilities by way of payment arrears accumulation. In spite of the escalation in the build-up of payment arrears, however, the government has consistently breached the ESAF/PRGF ceilings on the PSBR. The out-turn exceeded the programme ceiling by 61 percent in 1998 and by 89 percent in 1999. For the 2000 fiscal year the overrun was an astronomical 981 percent. The overrun in 2001, however, was a more moderate 27 percent.

Historically, the domestic banking system has been the largest source of official domestic borrowing by the government. This high dependence on the banking system for the government's fiscal operations has been a matter of considerable concern since it can potentially weaken monetary policy and increase the likelihood of rekindling inflationary expectations and inflation. In a complete departure from the past, government's domestic official borrowing in 2001 was mainly from the non-bank public.

The government also moved from being a net borrower to a net depositor with the banking system as a whole. In contrast to 2000 where government's net borrowing from the Bank of Ghana was about ₵1870 billion (equivalent to 6.9 percent of GDP), its accounts at the Bank at the end of the 2001 fiscal year showed an improvement in deposits of about ₵1180 billion (or 3.1 percent of GDP).

Finally, government's recourse to hidden liabilities to mask the fiscal stance seemed to have waned in recent years. Financing by way of net accumulation of payments arrears declined from a high of nearly 33 percent of total domestic borrowing in 1999 to 2.1 percent and 2.5 percent in 2000 and 2001, respectively.

- *Domestic Revenue*

Government domestic revenue comprising all tax and non-tax revenues — excluding proceeds from divestiture — and measured on a cash basis is an Indicative Benchmark in

the PRGF Arrangement with the IMF. A fiscal criterion — measured by the ratio of domestic revenue to nominal GDP — is also a key indicator in determining a country's HIPC eligibility. Under the fiscal criterion, a domestic revenue/GDP ratio of 15 percent is the minimum required to be eligible for the HIPC Initiative. The domestic revenue/GDP ratio for Ghana at Decision Point (based on performance at the end 2000) was 17.7 percent of GDP. This improved to 18.2 percent of GDP for the 2001 fiscal year. All the major categories of tax revenue contributed to the improved outcome. Non-tax receipts as a share of GDP, however, declined.

- *Domestic Payments Arrears*

Two observations can be made in respect of domestic payments arrears. First, there was more clearance of the existing stock in both 2000 and 2001 compared to the preceding two years. Secondly, the process of arrears accumulation continued in both 2000 and 2001, albeit at a reduced rate. As a result the net addition to the stock declined from an average of 2.8 percent of GDP for the 1998-1999 period to 0.2 percent and 0.1 percent of GDP for the 2000-2001 period.

It is important, however, to stress that the reasons for the developments in 2000 are quite different for those for 2001. In the election year 2000 it was politically imprudent to entertain payment arrears. On the contrary, there was some premium to clearing the backlog. Government instead borrowed massively from the Bank of Ghana to finance its operations — 6.9 percent of GDP in 2000. The mode of finance — literally printing of large volumes of currency — resulted in increased inflation, which rose to 40.5 percent at the end of 2000 (year-on-year basis) compared to the reported 13.8 percent at the end 1999 and 21.3 percent at the end of 2001.

By contrast, the decline in the rate of net build-up of the arrears stock in 2001 was made possible because of a much favourable net foreign inflow position — estimated at 8.3 percent of GDP in 2001 compared to negative 0.3 percent of GDP (a net outflow) in 2000 — what has mostly been discussed elsewhere as exceptional finance attributable to the democracy dividend.

- *Interest Payments on the National Debt*

Interest due on the national debt (domestic and foreign), as was the case in 2000, was the single largest item of government expenditure for the 2001 fiscal year. The payments of 8.5 percent of GDP represented 44.5 percent of recurrent expenditures compared to the 2000 outcome of 7.5 percent of GDP, which accounted for 40.4 percent of the recurrent expenditures. Thus the perennial crowding-out of non-interest expenditures seems to have persisted in 2001 and with relatively much higher intensity than was the case in 2000.

- *Public Expenditure Management (PEM)*

Weak systems of commitment control and internal audits as well as the absence of reconciliation between budget and banking data continue to undermine the effective execution of the budget. These weaknesses, together with difficulties with the payroll system, — the “ghost names” phenomenon — have led to a substantial stock of payments arrears to the SSNIT, DACF, and GETF. The breakdown in the processes for reconciling fiscal and banking data, and the proliferation of bank accounts outside the control of the Controller and Accountant General’s Department (CAGD) increase the risk of inappropriate use of budgetary resources. Reporting systems are also weak with most MDAs failing to submit monthly reports on budget implementation to the CAGD. Reports submitted also suffer from problems of timeliness, scope of coverage, and accuracy. They also fail to capture the internally-generated funds (IGFs) of ministries, departments, and agencies (MDAs) and many donor aid flows, especially those in respect of project grants and loans. In 2000, for example, the CAGD’s system failed to capture expenditures equivalent to 6.6 percent of GDP.

There are indications of serious attempts being made to improve the PEM system. The success of the PEM among other things, would depend on the following:

- an effective expenditure control system at the commitment stage;
- a fully operational MTEF involving all MDAs and the District Assemblies;
- willingness of donors to let go of their “pet” projects and channel grant-supported projects through a centralised pool for proper co-ordination; and

- timely identification, accurate costing, proper sequencing and prioritisation of projects must emanate from the GPRS so that the expenditures that feed the PRGF and the Budget are consistent with the triple objectives of macrostability, employment-generating economic growth, and poverty reduction.
- *Distribution of Cocoa Proceeds*

The share of farmers' income in the total proceeds was 44 percent — lower than projected 63 percent and, even more importantly, lower than the 62 percent realized in year 2000.

The disturbing development is that the reduced farmer share of the proceeds was not to the benefit of government tax revenue. In fact, the tax share realized of 10 percent was lower than the targeted 11.3 percent, which was also the realized share in year 2000. The benefits all accrued to the purchasing and marketing companies – comprising Cocobod and the licensed buying agencies (LBAs).

The perennial problem arising from the lack of transparency in the Cocobod financial operations (not helped any by the LBAs) including the “special” taxed rates accepted by Cocobod from the Bank of Ghana comes strongly to the fore, crying out for rectification.

Money, Credit and Prices

The tough monetary policy stance of the new administration of the New Patriotic Party (NPP) was dictated by the poor inheritance bequeathed to them by the government of the National Democratic Congress (NDC). With year-on-year inflation at over 40 percent at the beginning of the year, and a clear indication of injection of over 900 billion cedis into the economy in the third quarter of 2000 alone, a contractionary monetary policy was called for to mop away the excess liquidity and to bring inflation in check.

A huge domestic debt overhang set the second agenda for a tough monetary policy stance. Central Government gross domestic bonded debt alone stood at over 25

percent of national output and 123 percent of total budget revenue at the close of 2000. Interest payment on the debt was about 15 percent of total expenditure: more than the allocation for development expenditure, and greater than the total of the expenditure on health and education combined. With the fiscal being structurally out of gear and the government continually having to borrow to service the debt, interest rates were kept perpetually high. Further, a large chunk of the debt was of short-term nature, rendering new borrowing only sufficient for debt servicing.

Thus, monetary policy needed to be designed to (a) mop-up excess liquidity in the economy to lower the rate of inflation; (b) lengthen the maturity of the debt, and work in tandem with prudent fiscal management to lower the debt burden; (c) lower interest rates to encourage investment and boost output; and stabilize the exchange rate.

Inflation continued to be the ‘public enemy number one’. Thus the main thrust of monetary management was to bring down the level of inflation and to arrest the fast depreciating currency. The monetary authorities therefore continued with their contractionary monetary policies as they had done since 1994, except for occasional liquidity binges during election years.

The Bank of Ghana continued to rely on the rate of interest as the main monetary instrument with the Reserve Money as an intermediate target. Targets for Reserve Money were set within the IMF programme agreed in 1999. Thus with quantity (reserve money) fixed, the price level (interest rate) is left to be determined by the money market forces of demand and supply.

Except for the last quarter of the year, the Bank of Ghana religiously kept within the reserve target limits. Interestingly, the banks did not alter their portfolio behaviour as can be seen from the unchanging nature of the primary and secondary reserve ratios. The actual primary reserve holding of the banks was the same when the mandatory requirement was increased to 9 percent as when it was at 8 percent. Obviously, the

squeeze on the money supply as reflected in the changes in the money multiplier was the result of portfolio changes of the non-bank public.

The persistently high rates of interest on Treasury bills were responsible for the unwillingness of the banks to alter their portfolio behaviour. Ghana, like most developing countries, is confronted with a structural deficit: a weak tax-base and the resultant weak-revenue is never enough to match national expenditures. The resulting deficit is then financed by borrowing or fiduciary issue. Borrowing internally through the sale of Treasury bills on the open market at the Bank of Ghana creates domestic debt. By the beginning of 2001, this Government bonded debt had scaled the 9 trillion cedis mark. Worse of all, much of this debt was of short maturity. At the beginning of 2001, the interest on the domestic bonded debt was about a third of total recurrent expenditure. New borrowings by Government were therefore only to finance interest payments on the domestic debt. This exerted upward pressure on the rate of interest. Thus from a level of 34.18 percent in the first quarter of 2000, the 91-day rates went up to 47.15 percent by the second quarter of 2001 before finally dropping to close the year at 28.94 percent.

The fall in the rate of interest at the close of 2001 was a result of the decisive action by the authorities to adopt and implement recommendations from the National Economic Dialogue to extend the maturity of the domestic debt. The Bank of Ghana introduced the first ever Government of Ghana Inflation Indexed-Linked Bonds (GGILB) on to the money market. The launch of the inflation-index bonds was to create an atmosphere for government to convert a portion of its short-term domestic debt into medium-term to ease interest payments and reduce excessive short-run borrowings by Government. At the inception of the GGLIB, banks were required to hold at least half of their secondary reserve requirements in the bonds. This action led to a decline in the short-term Treasury bill rates as demand pressure eased up.

The introduction of the Indexed-Linked Bonds changed the face of the money market in Ghana. Before then the money market had only a few instruments of short-term nature—91-day and 182-day Treasury bills and 1-year Treasury notes. From ₵149.6

billion in September, the government had raised as much as $\text{¢}1,045.2$ billion from the sale of GGLIBs by the end of 2001. However, this was mainly due to compulsory acquisition by the banks.

In 1998, the Government of the NDC set itself a short-run objective of running inflation down to single digit level. Thus, in May of 1999 when the rate of inflation dropped to 9.4 percent the Government applauded. CEPA had pointed out earlier the likely trade-offs in moving inflation in a developing country down below certain levels.

Naturally, the new administration of the NPP set price stability as one of its prime targets. The new administration, however, has good fortune behind it. Inflation had reached its cyclical peak around the end of 2000, but the political change extended the peak to the end of the first quarter of 2001. Since April 2001 inflation has been on the decline, and continued to decline to a low of 21.3% by the end of 2001 (see Table 4.4). As was to be expected the average inflation lagged behind the year-on-year inflation. Average inflation therefore increased from 25% in December 2000 and peaked at 37.7% in August before beginning a descent to 32.9% by the end of the year 2001.

Clearly, the goodwill enjoyed by the New Patriotic Party administration in the first six months of 2001 helped to stabilize prices. Even before the exchange rate would show signs of stabilizing, spare-parts dealers and other members of the Ghana Union of Traders Association (GUTA) decided to lower some of their prices as a show of goodwill towards the new government.

External Sector

Developments in the foreign exchange market in 2001 were similar to those of 1998. A relatively stable exchange rate, depreciating by only 5.3 percent on a year-on-year basis in 2001 compared with 4.2 percent in 1998, and a relatively higher first half year depreciation, to be followed by a second half year depreciation of about 1 percent in each year. In spite of the similarities in outcomes, the causes and possibilities of

sustaining the outcomes were different. In the one case, stability was maintained by favorable external conditions that were used to support the currency and subsidize imports. In the other case, a drop in inflationary expectations following a new government and a fiscal policy that depressed aggregate demand, as well as increased external inflows – exceptionally favorable aid flows and debt deferment – were responsible.

In spite of one of the worst trade performances, a substantial increase in external assistance led to an improvement in the balance of payments situation with gross international reserves increasing slightly from one month (four weeks) of imports cover in 2000 to 1.3 months (seven weeks) of imports cover in 2001. Exceptional programme support, consisting of programme grants, concessional loans and deferred loan repayments, increased by three hundred and sixty four million dollars (US\$364 million). These flows moderated the adverse effects of the poor performance of Ghana's traditional exports on the balance of payments.

Ghana's traditional exports consisting of gold, cocoa and timber did poorly in 2001 as a result of both low volumes and prices in the world market. Gold exports in value terms declined by 12 percent to the lowest value of US\$617.8 million since 1998. Cocoa exports also decreased in value terms by 12.5 percent to the lowest value in the last ten years. Similarly, the value of timber and wood products exports decreased by 3.4 percent. This poor performance of the traditional exports was moderated by better performance of the non-traditional exports, which increased by 15 percent in 2001 resulting in overall export earnings declining by only 3 percent.

The combination of decreasing exports values and increasing imports led to one of the worst trade deficits in terms of percentage of GDP. The trade deficit in terms of GDP, increased from 15.3 percent of GDP in 2000 to 16.7 percent in 2001. In spite of the poor trade performance, the current account deficit (excluding official transfers) decreased by about 18 percent on account of a 38.2 percent increase in net private transfers.

The Ghana Poverty Reduction Strategy Paper (GPRS)

The poverty reduction strategy paper, known in Ghana as the Ghana Poverty Reduction Strategy Paper (GPRSP), is one of three components of the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative. The first component of the enhanced HIPC Initiative is the calculation of debt relief based on debt sustainability analysis. The second is the poverty reduction strategy paper (PRSP). This was not initially part of the HIPC Initiative, but introduced in 1999 in response to demands to link debt relief to poverty reduction. The third is the Poverty Reduction and Growth Facility (PRGF) of the International Monetary Fund (IMF). This is the economic reform programme that is expected to inform, in particular, macroeconomic policy implementation during the HIPC Initiative process.

The introduction in 1996 of the Heavily Indebted Poor Countries Initiative to provide debt relief to low income countries was due to a combination of three factors. The first was pressures from non-governmental organisations, led by Jubilee 2000, for debt relief. The second was the implementation of the Brady Plan that provided debt reduction for middle-income countries and the third was the fact that a number of low income countries were not servicing their debt anyway. The HIPC Initiative aims at bringing down selected debt burden indicators to what is perceived to be sustainable levels.

The HIPC Initiative has undergone some change since it was introduced in 1996. With the changes made in 1999, Ghana became eligible for debt relief under what is now known as the Enhanced HIPC Initiative.

To be eligible for debt relief under the HIPC Initiative a country must qualify for concessional assistance under the IMF and World Bank. In addition it must face an unsustainable debt service even after the application of traditional debt relief mechanisms, establish a track record of reform and sound policies under IMF and World Bank supported programmes and have prepared a poverty reduction strategy paper.

To benefit from debt relief under the HIPC Initiative there are two critical stages that the eligible country needs to go through. The first is to reach the decision point and the second is the completion point. The evolution of the HIPC Initiative since 1996 has not changed the need for a country to go through these two critical stages.

At its introduction the HIPC debt relief was lauded by many in the international community. It was seen to be providing a comprehensive and integrated framework and it was extended to multilateral creditors. However the Initiative soon ran into a lot of criticism.

A review of the HIPC Initiative was conducted jointly by the World Bank and the IMF in 1999. In July of that year, the joint staffs of the two organisations presented a paper on modifications to the HIPC Initiative. The modifications addressed several of the issues that had been pointed out as weaknesses of the strategy.

It was envisaged that these modifications would increase the number of countries that would qualify for HIPC assistance. Indeed Ghana was one of the countries that became eligible for consideration for debt relief due to the enhancement of the HIPC Initiative. The changes were also expected to provide more debt relief to the participating countries. Whether or not poor countries will truly benefit from debt relief depends on whether the funds that should have been paid out as debt relief are actually available to the country. If a country is in chronic arrears then the debt relief simply relieves the country of a debt obligation rather than actually make available finances to be used for other purposes. A possible advantage of the enhanced HIPC Initiative under these circumstances is that policy may become more poverty-focused.

The debt relief that is provided, however, is limited and there is not much in the way of additional funding. There is evidence that donor countries are reducing aid flows at the same time debt relief is granted. Overseas development assistance to Africa fell in per capita terms in the 1990s. In the case of Ghana official aid disbursement from the Development Assistance Committee Countries stood at US\$468.67 million in 1990. It

rose to US\$505.04 million in 1991, the highest value in the 1990s. It averaged US\$238 million between 1992 and 1997. There has been an increase in disbursements since 1998 from US\$290 million to US\$319 in 1999 and a drop to US\$315.86 in 2000.

The expectation that there would be a fundamental difference between the PRGF and ESAF has not materialised. The macroeconomic framework has not changed in any significant way since the start of the enhanced HIPC Initiative. Indeed some commentators argue that there may be very little scope for variation between the Enhanced Structural Adjustment Facility and the Poverty Reduction and Growth Facility.

Some observers have argued for a delinking of debt relief and the poverty reduction strategy paper. They recommend a less complex type of conditionality. A Poverty Fund should be set up to receive all the funds released due to debt relief. Guidelines could be set as to how the funds are utilised and an entity created to disburse and monitor the use of the funds.

The HIPC Process

Although Ghana was eligible for debt relief under the enhanced HIPC Initiative in 1999, it was not until 2001 that the Government opted for debt relief under the Initiative. When Ghana became eligible for HIPC debt relief in 1999 its debt burden indicators were not significantly above the critical values. The amount of debt relief that Ghana would have qualified for was therefore not very large. Opting for the HIPC option was therefore not attractive given the “costs” of going HIPC. One of such costs was Japan’s warning that Ghana would no longer be eligible for loans.

The amount of debt relief that Ghana is expected to receive under the enhanced HIPC Initiative is calculated on the basis of the fiscal criteria. Ghana would get little relief if the export criterion had been used because its export to debt ratio is only 7 percentage points above the critical value. It is estimated that the total debt relief required to bring down the net present value of the ratio of debt to revenue to below the critical

value of 250% is US\$2186m. The enhanced HIPC relief is expected to reduce debt service payments due by about US\$215m per year on average between 2002 and 2011. In 2002 the debt relief for Ghana is US\$249m. It is made up of US\$153m of traditional debt relief and US\$96m of HIPC relief. Twenty percent of the HIPC debt relief is to be used for domestic debt reduction and the remaining 80% is earmarked for poverty reduction programmes and activities.

To arrive at completion point Ghana is expected to have undertaken certain actions and achieved specific targets. These trigger points were identified by “drawing on the priorities identified in the draft GPRS”. Considering that by April 2002 the process of prioritising the GPRS had not been completed the basis of the choice of these trigger points is unclear.

Assessing the GPRS

The main goal of the GPRS is to “ensure sustainable equitable growth, accelerated poverty reduction and the protection of the vulnerable and excluded within a decentralised environment”. The document sets out a number of poverty and growth targets that are to be achieved between 2002 and 2004. Ghana’s long-term poverty reduction strategy “is to achieve growth to ensure the virtual disappearance of poverty by 2020 as originally set forth in *Ghana Vision 2020*”. It is recognised in the document that poverty reduction requires not only an increase in growth rates but also the “implementation of public policies for drastic spatial reorganisation of investment for economic activity and social protection”.

The GPRS has a very broad scope. This is not surprising since poverty is a multi-dimensional phenomenon and to address it requires a broad frontal attack. Indeed this is what the GPRS attempts to do with over 200 targets set out among the five thematic areas that it addresses. Some of these targets are quantified and some by their nature cannot be. The very broad focus of the GPRS raises the question of whether the targets can be

achieved in the time frame set and whether the resources, both financial and human are available to achieve the objectives within that time frame.

The Government's priorities raise questions about what the contents of a pro-poor growth strategy should be and it also raises the issue of sequencing. The GPRS has tried to address the issue of the content of the pro-poor growth strategy by suggesting the proportion of spending that should go to measures that directly impact the poor and those that do not. Having said that, there is still a tension in the GPRS that is again manifested in the Government priorities, between poverty reducing measures and growth promoting measures. The high incidence of food insecurity amongst most of the poor and the imbalances in access to quality education, safe drinking water, roads and other physical infrastructure for example, underscore the need to avoid a development strategy that emphasises growth and depends on the trickle down of benefits of that growth. Growth is necessary but not sufficient for poverty reduction.

Economic Outlook

Under the PRGF the central goal of economic policy management is poverty reduction and growth, not necessarily in that order. Nevertheless, this is the "what ought to be". This understanding is very important in terms of economic management as the goal posts shift from ESAF to PRGF. Under the former, monetary policy played a central role together with fiscal and exchange rate policy in the achievement of the goal of macroeconomic stability. Within the context of the PRGF, monetary policy has a dual role. First, as an adjunct player in the achievement of the main objective of poverty reduction and growth; and second, as a principal player in the maintenance of macroeconomic stability, which is a necessary condition in the achievement of poverty reduction and growth.

Arguably, the institution of the monetary policy committee (MPC) of the Bank of Ghana could serve to bring about the requisite balance. Though this seven-man committee is dominated by officials of the central bank and has the Governor as its chairman, there are precedents in Nigeria and the UK, which give cause for warranted

optimism. Under the Bank of Ghana Act 612, Section 27, the MPC is charged with (i) initiating proposals for the formulation of the monetary policies of the bank and (ii) providing the statistical data and advice necessary for the formulation of monetary policies.

Under the PRGF, “the monetary targets for 2002 are designed to achieve the targeted reduction in inflation to 13 percent while rebuilding gross foreign reserves to 2 months of imports by end-year.” To this end the authorities expect a contraction in central bank’s net domestic assets through repayments by government. This harnessing of fiscal policy to serve the purposes of monetary policy is strategic and critical to the realization of the expectation of “nominal interest rates to fall broadly in line with inflation”.

By July 2002, inflation already within sight of its marked target seemed likely to over-perform by the close of the year. It is, however, not clear what is driving the rate of inflation down. Monetary policy remains very contractionary as planned, and deficit financing seemed to have been limited to interest expenditures.

Yet still, the drive down in the rate of inflation could just be following a path in the familiar 3-year inflation cycle to which attention has been drawn above. If the latter is the case, then June or July 2002 marks the trough of the inflation cycle and the country should prepare itself for an ascent.

Leaving aside the apparent subordination of the objectives of fiscal policy — growth and redistribution — to those of monetary policy — specifically disinflation and financial sector stability — there is the issue of the attainability of the programmed fiscal outcome itself. The achievement of the fiscal targets for 2002 will depend critically on the improved effectiveness of public expenditure management (PEM) system and the raising of additional government revenue equivalent to 1.0 percent of GDP. In what follows the searchlight will be thrown on the targets set for the DPB and the PSBR and their components.

The effectiveness of the PEM will depend on a number of identifiable factors several of which are unlikely to be satisfied during the 2002 fiscal year. The lower than likely expenditure targets, combined with an inadequate PEM system — especially at the commitments stage — would either perpetuate the payments arrears phenomenon, or lead to arbitrary and possibly counterproductive cutbacks and/or postponement of expenditures critical to the objectives of growth and poverty reduction.

Realising the programme targets, however, would also require that delays in respect of aid disbursements are kept to a minimum and interest payments on the domestic debt stay within the programme target. The non-functioning of the automatic pricing formula for petroleum products and the delay in implementing the recommendations for the institution of the petroleum debt service charge, however, have led to the continued build-up of the TOR debt. Should the government take over this debt, as appears unavoidable, the resultant interest payments will potentially affect the size of the OBB deficit and thus the PSBR. This is further compounded by the funding of subsidies occasioned by delays in moving to full cost recovery tariffs for water and electricity.

On the strength of the available information, therefore, the fiscal objectives for 2002 are clearly not achievable. This raises serious questions about the consequences of an enforced attainment of the monetary targets, as this could mean even greater pressure on the fiscal than programmed.

The external debt repayment of US\$228 million deferred in 2001 is expected to be repaid over the next five years as follows:

- 2002—US\$30 million;
- 2003—US\$60 million;
- 2004—US\$58 million; and
- 2005—US\$55 million
- 2006—US\$25 million

In addition to these Ghana's medium term development objectives and contractual obligations require that external reserves will be built up over the next five years, reaching about four months of imports cover by end-2005.

The achievement of these requirements will depend on trade performance, aid flows, and the accompanying macroeconomic policies, including exchange rate policy. Ghana's trade performance can be expected to improve over the next few years both on account of favorable world market prices and the volume of traditional and non-traditional exports. The current high prices for cocoa are expected to continue for a while. Gold prices have also risen and are expected to remain above the US\$300 per ounce mark.

On the production side, traditional export volumes will increase. It is expected that after three years of mass spraying of cocoa farms some results will begin to show in 2003. For the current year, however, the projected volume is proving overoptimistic. Apart from possible increases in production from old mines, some new mining operators such as Sian Goldfields Limited and Kibi Goldfields may come on stream, increasing gold production and exports. These may be realized from the fourth quarter of 2002.

Oil prices averaged US\$24.4 per barrel in 2001. Brent crude for June 21, 2002 closed at US\$24.5 per barrel, close to the annual average of 2001. In spite of some fears about developments in the Middle East, crude oil prices are unlikely to rise substantially above last year's average. Russia, for example, seems to be targeting a price between US\$20 per barrel and US\$25 per barrel.

Operationalising the GPRS will require its translation into the national budget and the budgets of the MDAs. The GPRS is fairly explicit on the pattern of expenditure that should exist by the end of the three-year period. However, the GPRS priorities cannot be reflected in the budget overnight. As the document rightly states: "There are rigidities, which limit adjustments to the sectoral composition of expenditure in favour of poverty reduction and growth in the medium-term." Some of these rigidities identified in the

GPRS are the large share of public salaries in the budget and on going projects and programmes that cannot be aborted mid-stream. There has been some realignment in the 2002 budget towards an increase in the proportion of discretionary expenditures for the social sector. Some of this success has been achieved through re-classification of expenditures.

For the poverty reduction objectives to be achieved there is an urgent need for targeting of interventions. An equal distribution of the HIPC resources amongst regions and districts is not acceptable. Some districts and sub-districts are in more urgent need of resources than are others. It is necessary that the resources be allocated within the reach of poor people and communities. It is imperative therefore that the recommendation in the GPRS that District Assemblies should be used to assist in identifying sub-regional areas of deprivation be implemented now. Following on from this a district level database must be created for effective targeting of interventions.

The framers of the Poverty Reduction and Growth Facility expect it to be prepared using a transparent process involving the participation of civil society. Civil society also has an important role to play in monitoring and evaluation implementation of the GPRS. These are important challenges that raise several issues such as:

- Broad agreement as to what constitutes “participation” in Ghana. The process of preparing the GPRSP has been criticised in some quarters as not being participatory enough, if at all.
- One of the important stakeholders in the poverty reduction process is the very poor. How can they be incorporated into the process? How can they be made effective participants in the process and not just be a “show piece”?
- Permanent structures need to be developed to facilitate the process of dialogue and consultation. The District Assembly is the most obvious institution at the local level for this purpose.

Effective use of existing capacity is constrained by a lack of data with which to conduct analysis. The most recent household survey is now almost four years old. It is

important that the planned surveys, i.e. the fifth Ghana Living Standards Survey and the second Core Welfare Indicators Questionnaire, are phased and implemented so as to provide the necessary information to conduct the analysis and provide the information needed to inform policy.