

## ***Managing an Economy in a HIPC-Constrained Environment***

In February 2001, Ghana formally opted for the enhanced Highly Indebted Poor Country (HIPC) Initiative of the Bretton Woods Institutions (BWIs). The HIPC initiative was up by the rich nations in 1996 through the IMF and World Bank and calls for the reduction of external debt through write-offs by official donors. Of the initial 41 countries targeted for relief under this initiative, 33 are in Africa. For these countries, it was realized that even full use of traditional mechanisms of rescheduling and debt-reduction may not be sufficient to lead them to sustainable external debt levels within reasonable period of time. To qualify for relief under HIPC the country must do the following:

- Adopt a Poverty Reduction Strategy Paper (PRSP) through a broad-based participatory process, by the decision point
- Make progress in implementing the PRSP for at least one year by the completion point
- Have a program with the IMF and the World Bank
- Face unsustainable debt burden, beyond debt-relief mechanisms such as Naples terms (where low income countries can receive a reduction of eligible external debt of 67% in NPV terms).

When a country satisfies some of the initial conditions it is said to have reached decision point and qualifies for some relief under the initiative. If at this point, the country manages to keep a track record of good performance, then it gets more benefits. It is possible under this phase for countries to obtain up to 90 percent reduction in the present value of their debt. When the country finally reaches the **completion point**, then it gets full benefits under the HIPC initiative.

Ghana, with a population of around 20 million and a per capita income of about \$300 is certainly a poor country. A little arithmetic will show that the average Ghanaian lives under one dollar a day! Household Living Standards Survey carried out by the Ghana Statistical Service in 1998/99 estimates that about 40 percent of Ghanaians are poor, down from a level of 53 percent in 1992. The majority of the poor are rural folk engaged in food production.

Ghana is also a heavily indebted country. At end-2000, the total public external debt stock was estimated at US\$5.9 billion in nominal terms, including US\$40 million of arrears. Total debt is estimated in NPV terms at US\$3.8 billion, equivalent to about 558 percent of government revenues, about 152 percent of exports of goods and nonfactor services, and about 77 percent of GDP. Of the total debt 52.1 percent was owed to multilateral creditors, and 47.9 percent to bilateral and commercial creditors. IDA, AfDB and IMF account for 93 percent of multilateral debt. Japan and the United Kingdom are the largest bilateral creditors with respectively 60 and 10 percent of the bilateral outstanding debt. The Commercial debt amounts to US\$348 million in nominal terms of which Samsung Corporation of Korea is the largest creditor with 37 percent of the outstanding commercial debt in nominal terms. This debt was contracted by the Tema Oil Refinery (TOR) and is collateralized against TOR's assets. The debt is largely owed by the central government with a share of 58 percent of the outstanding claims, and the remaining 42 percent is owed by two public corporations, TOR with a share of 37 percent and Ghana Telecom with a share of 5 percent.

As fate would have it, on January 7<sup>th</sup> 2001, Ghana crossed a critical landmark in her political history. For the first time since independence in 1957, there was a smooth change over of governance from one elected party to another. The significance was not only in the fact that an elected government completed its term of office, but also that another party, through the ballot box, took over the reins of government. The new Government which took over in January 2001, was bequeathed a rather poor inheritance: High and accelerating rate of inflation, high interest rates, large fiscal imbalances, huge debt burden, external reserves the equivalent of about a month and a half cover, depreciating exchange rate, and rising unemployment for both skilled and unskilled labour. This was certainly not a healthy base to deliver any campaign promises. Going HIPC was to give the government a "breathing space" so as to be able to reorganize itself.

The amount of debt relief that Ghana is expected to receive under the enhanced HIPC Initiative was 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 was 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\$2,186m. 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 2001, Ghana obtained relief under the initiative to the tune of about \$190 million, but this was mostly the traditional debt relief. 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.

At a press conference in August 2002, the Finance Minister announced that \$36.9 million out of the total amount has been lodged in the HIPC account. It is in the sharing of the HIPC money that the politics took over from the economics.

Recollect that one of the basic requirements of the HIPC is that the country draws up a Poverty Reduction Strategy Paper which is to guide how the HIPC money will be expended. The Ghana PRSP, known as 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. The projects set out within the GPRS were to have been costed so that when HIPC funds become available it can be easily channeled into a specific poverty reduction project. So either the projects have not been properly identified and costed or that we allowed the politics to take the better part of us and so just shared out equal amounts to each district and asked them to find projects. If the GPRS was carried out on consultative basis with inputs from the districts why don't we know the projects we are to support?

The biggest challenge under the HIPC is actually in terms of economic management. The initiative comes with a Growth and Poverty Reduction Facilities which creates the triggers by which the country is monitored. Within this framework, the country is expected to achieve the triple objective of macrostability, growth, and poverty reduction. Unfortunately, it is

difficult for a HIPC constrained economy like Ghana to achieve the three objectives simultaneously.

Macroeconomic stability may call for certain fiscal and monetary policies that will compromise on the growth objective, or the poverty objective or both. For example, fiscal restraint can lead to the withdrawal of certain public services and this can hurt the poor. Or, a monetary restraint that leads to increases in interest rates to squeeze credit expansion may also hurt investment and compromise on the growth objective. Meanwhile these are the very triggers by which our ability to reach the completion point in the HIPC initiative will be judge.

There are serious challenges for the country. Ghana must endeavour to generate enough of domestic revenue and wean itself away from this donor-dependence syndrome to get the true needed relief. For as has been said “debt is not a financial or an economic problem at all, but in every way a political one. It is the best instrument of power and control of North over South ever invented; far superior to colonialism which requires an army, a public administration and attracts bad press. Control through debt not only requires no infrastructure but actually makes people pay for their own oppression”.