Economic and Market Insight

Policy Update: Ghana Secures IMF Board Approval for the 3-Yr, US$3 Bn Programme supported by the Extended Credit Facility

GCB CAPITAL LTD
Research & Analytics

May 2023

Ghana Seals Board-Level Approval for a 36-Month Programme Supported by an Extended Credit Facility

After almost 11 months of negotiations with the International Monetary Fund (IMF) for a programme to restore macroeconomic and debt sustainability, the IMF Executive Board approved the US$3bn (SDR 2.242bn | 304% of Ghana's quota with the IMF) package supported by the Extended Credit Facility (ECF) for Ghana on May 17, 2023. The 36-month arrangement came within 156 days of Ghana reaching a Staff-Level Agreement (SLA) with the Fund on December 12, 2022. The approval signals the programme's official start and will trigger an immediate disbursement of SDR 451.5 Mn (about US$600 Mn) under the programme. According to the IMF, the programme will build on the government's Post COVID-19 Programme for Economic Growth (PC-PEG), focusing on restoring macroeconomic stability and debt sustainability along with wide-ranging economic and structural reforms to build resilience, laying the foundation for stronger and more inclusive growth. The approval of the programme is the first necessary step towards rebuilding the macroeconomic fundamentals and setting the stage for robust and inclusive growth.

The programme envisages large and frontloaded fiscal adjustments based on significant revenue growth: Given the pronounced fiscal imbalance characterised by a large primary deficit since 2020, the fiscal strategy envisaged large and frontloaded fiscal adjustments. As an anchor, the government targets a surplus primary balance (on a commitment basis) of 1.5% by 2025, and to be maintained until at least 2028. The fiscal strategy hinges primarily on significant revenue growth supported by expenditure controls. In particular, the programme targets a revenue-to-GDP ratio of 18.7% by 2026 (from 15.7% in 2022), translating to a fiscal adjustment equivalent to 3% of GDP, which accounts for nearly 60% of the total adjustment required to achieve the programme target by 2026. The revenue interventions will include new taxes and the revision of existing tax handles. On the expenditure side, we expect a renewed focus on priority programmes and projects with high multiplier effects and far-reaching social impact, enhancing efficiency and transparency in the public financial administration and strategies to reduce contingent liabilities from the SoEs sector. Structural reforms to tax policy, revenue administration, and public financial management framework will complement this frontloaded fiscal consolidation drive envisaged under the programme.

The Scope of Fiscal Adjustment Envisaged Under the Programme

	2022E	2023F	2024F	2025F	2026F
Revenue & grants (% of GDP)	15.7%	16.8%	17.3%	17.8%	18.7%
Primary Bal. (non-oil) (% of GDP)	-5.6%	-3.1%	-1.7%	-0.5%	-0.5%
Primary Balance (% of GDP)	-3.6%	-0.5%	0.5%	1.5%	1.5%
Primary Balance (cash) (% of GDP)	-0.8%	-1.2%	-0.2%	0.9%	0.9%
Nominal GDP (GHS'Bn)	615.26	873.4	1,077.4	1,251.5	1,413.8

Source: IMF

Already, the government increased the VAT rate by 2.5% in the 2023 budget, rolled out the new property rate collection system on a pilot basis, implemented three (3) new tax bills that could rake in about GHS4Bn in 2023, increased utility tariffs (water, electricity -2x and gas), reversed the benchmark value discount policy completely and intensified revenue assurance and compliance enforcement among other revenue interventions as part of the revenue growth strategy. The government expects these new revenue measures to rake in about 1% of GDP (about GHS 8.73 Bn) in additional revenue for 2023. The expenditure control efforts also target project reprioritisation to reduce CAPEX, limit wage growth and new hires, rationalise expenditure on public sector goods and services, and reduce transfers to statutory funds. As an additional layer, the authorities expect to complement these measures with strict expenditure and commitment controls.

The Impact of the New Revenue Measures

Revenue Measure	**Impact (% of GDP)**
2.5% increase in VAT to 15%	0.3
Reversal of benchmark discount	0.2
Revision of income-based tax	0.2
Extension of the national fiscal stabilization levy	0.1
Reform of the E-levy	0.1
implementation of the e-VAT	0.1
Revision of excise taxes and VAT exemptions	0.1
Erosion of revenue due to inflation	-0.2
Total	**1.0**

The Domestic Debt Exchange Programme (DDEP) was a first step towards restoring fiscal and debt sustainability, and we expect the government to resume the conversation on the second leg of the DDEP to cover Cocoa bills, domestically issued dollar bonds and pension funds exempted from the earlier exchange. We expect the government to follow on the heels of the financing assurances to commence negotiations with external creditors targeting about US$10.5 Bn in external debt service relief during the programme. While the delays in the debt restructuring conversation for Zambia, Chad and Sri Lanka are a source of concern, we expect the progress made on those negotiations to shape the narrative around Ghana's attempt to seal a deal with creditors under the Common Framework.

A complementary monetary policy stance is required to anchor disinflation and Cedi Stability: While a disinflationary process is underway, and inflation has eased for four consecutive months in 2023, at 41.2%, headline inflation is still 31.2% outside the upper band of the 8%±2% medium-term inflation target band with emerging upside risks from the price effects of the new revenue measures upward utility tariff adjustments. Thus, an appropriately tight monetary policy stance may be required to anchor inflation expectations, tighten the grip on inflation and sustain the disinflationary process. The formal start of the IMF programme has also kicked in the Memorandum of Understanding between the Central Bank and the Treasury on zero deficit financing under the programme, which should further strengthen the grip on inflation.

The Bank of Ghana's accelerated FX market intervention at the peak of the exchange rate crises also resulted in a sharp deterioration of Ghana's gross FX reverses. We expect the Balance of Payment (BoP) support under the programme and its catalytic effects to unlock additional sources of concessional financing tied to the programme to improve government financing, which should help in enforcing the MoU on zero deficit financing and improve FX liquidity on the domestic market in the near-term. With these interventions, we expect the BoG to revert to an increasingly flexible exchange rate regime to accelerate reserve accumulation.

The outlook for GDP growth dims in the near term: We expect the frontloaded fiscal consolidation envisaged under the programme, the impact of DDEP on the Bank's asset quality and credit stance, the heightened inflation risks and the highly unfavourable external market conditions to dim the growth outlook in the near term. Already, GDP growth softened to 3.1% y/y in 2022 (from 5.1% in 2021) and could further ease below 2% in 2023 before recovering steadily to around 5% by 2025. The outlook hinges on successful programme implementation relative to the set targets. A strong performance during the initial reviews will resonate with the market, potentially leading to a rating upgrade necessary to induce FDI flows. A speedy external debt restructuring will also prove crucial for the growth outlook as the realisation of the anticipated interest savings is an important component of the financing mix for 2023 and beyond. The heightened inflation risk and Cedi vulnerabilities, potential spillovers from Geopolitics and commodity price shocks are potential downside risks to the growth outlook in the near term.

Outlook for Growth and General prices

	2022E	2023F	2024F	2025F	2026F
GDP at constant prices	5.4%	3.2%	2.8%	4.7%	5.0%
Non-extractive GDP	8.4%	1.9%	2.2%	4.4%	4.8%
Extractive GDP	-12.1%	12.7%	6.4%	6.5%	5.9%
Real GDP per Capita	3.3%	1.0%	0.2%	2.1%	2.3%
End period inflation	11.2%	29.8%	20.1%	10.9%	7.6%
Average inflation	12.6%	54.1%	15.0%	8.0%	8.0%

Source: IMF

Rebuilding the BoP accounts to at least 3 months of import hinges on the anticipated savings from external debt restructuring: The IMF projected that Ghana needs a total of US$15.06Bn in Balance of Payments (BoP) support for the duration of the programme (2023 to 2026) to rebuild the gross FX reserve cover of at least three months of imports by 2026 (according to the Fund's definition of reserves). Thus, the US$3Bn financing from the IMF accounts for only 20% of the estimated BoP needs for the period, with the World Bank also expected to disburse about US$1.6 billion to support the programme.

The projections, however, envisage about US$10.5Bn in external debt service relief for the period, accounting for nearly 70% of the estimated BoP needs. While additional flows from the African Development Bank and other development partners will ease the dependence on savings from external debt treatment in closing the BoP gap, a highly successful external debt operation is fundamental to rebuilding the external buffers.

Thus, the Cedi could face an uncertain outlook after the positive news effect wanes if the negotiations on external debt restructuring do not progress with dispatch as expected. We also anticipate that investors will look beyond the proposed reforms under the programme and consider actual performance in warming up to the sovereign. A sterling performance at the first review could lead to a rating upgrade which will enhance market sentiments and induce FDI flows to stimulate growth.

Estimated BoP Needs and Sources of Funding Under the Programme

	2022E	2023F	2024F	2025F	2026F
C/A Bal. (% of GDP)	-2.1	-2.8	-2.3	-2.4	-3.0
BoP Financing Gap (US$'bn)	-	4.2	3.3	4.3	3.3
IMF (US$'bn)	-	1.2	0.7	0.7	0.4
World Bank (US$'bn)	-	0.5	0.4	0.4	0.3
Residual Gap (US$'bn)	-	2.5	2.2	3.2	2.7
GIR (When gap is closed) (US$'bn)	1.4	1.7	3.3	5.5	7.8
Month of import cover	0.7	0.8	1.4	2.2	3.0

Source: IMF

Research Contacts

Courage Kwesi Boti
Economist/ Research Lead
+233302945848 |+233302945838
ckboti@gcb.com.gh

Fund Management Contacts

Afua Akyaa Osei
Vice President, Fund Management
+233302945848 |+233302945838
aaosei@gcb.com.gh

Wilson Kyeremeh
Portfolio Manager, HSG
+233302945848 |+233302945838
wkyeremeh@gcb.com.gh

Advisory & Capital Markets Contacts

Baffour Agyarko Kwakye
Vice President, Advisory & Capital Markets
+233302945848 |+233302945838
bakwakye@gcb.com.gh

Michelle Nana Ohenewaa Kitson-Amoah
Associate, Advisory & Capital Markets
+233302945848 |+233302945838
mnodadey@gcb.com.gh

Disclaimer

This Economic and Market Insight has been prepared by the Research & Analytics Desk of GCB Capital Ltd solely for information purposes and does not constitute any legally binding obligations on GCB Capital. Any views expressed are those of the Research & Analytics Desk. Any views and commentary in this investor note are short-term views of GCB Capital Ltd's Research & Analytics Desk from which it originates and are not a personal recommendation and do not consider whether any product or transaction is suitable for any investor.

Whilst the information provided in this document has been prepared by GCB Capital's Research & Analytics Desk based on or by reference to sources, materials that GCB Capital Ltd believes are reliably accurate, GCB Capital Ltd does not guarantee its completeness or accuracy. The message is for information purposes only as of the date hereof and is subject to change. It is not a recommendation, advice, offer or solicitation to the reader to buy or sell a product or service. We do not accept any liability for losses (direct or consequential) which may arise from making use of this note or its contents or reliance on the information contained herein.

All opinions and estimates are given as of the date hereof and are subject to change. GCB Capital Ltd is not obliged to inform readers of any such change to such opinions or estimates. This document does not purport to contain all the information that you may desire. In all cases, interested parties should conduct their own investigations and analysis of the transaction described in the document and of the data set forth in the document. It is recommended for interested parties to check that the information provided is in line with their own circumstances about any legal, regulatory, tax or other specialist or technical advice or services, if necessary, with the help of a professional advisor. This document is confidential and may not be reproduced or distributed in whole or in part without the prior written permission of GCB Capital Ltd.

49 Ndabaningi Sithole Rd

Labone, Accra