Ghana’s Economic Development Updates

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Ghana’s Debt Situation: Implications for the Attainment of the SDGs

Summary: As 2030 draws nearer and the world is edging towards the target date for achieving the Sustainable Development Goals (SDGs), a rapid pace for the goals is imminent. How fast countries accelerate acheivement of the goals is however highly dependent on their abilities to mobilize development finance. There is sufficient evidence on the huge financing gap and the huge invesment required for countries, including Ghana to stay on track towards the SDGs. Compounding the struggle to close the SDGs financing gap further is Ghana’s debt burden. Overcoming the debt burden in Ghana will unlock financing for development and expand private sector investment for SDGs. Using recent data, this brief sheds light on Ghana’s debt burden and implications on reaching the gloabally agreed development targets, the SDGs. The brief draws on other macroeconomic challenges such as inflation and also the depreciation of the national currency with crippling effects on debt servicing. All of these ultimately shrink the fiscal space for investment in the SDGs. By providing the context on the unsustainable debt situation in Ghana, the brief profers some solution pathways that will reduce the impact of the debt burden and free up fiscal space for investment in the SDGs. The solutions require both domestic efforts as well as international support given that many developing countries will continue to look outward, to foreign capital markets to meet huge funding needs for the SDGs.

Background/ Context

In recent years, Ghana's fiscal and debt sustainability has been eroded by rising government spending in the context of continuous low domestic resource mobilization. Ghana’s debt as a proportion of its GDP has increased drastically over the last two decades. Figures from the International Monetary Fund (IMF) show more than a 100 percent increment between 2010 and 2022.

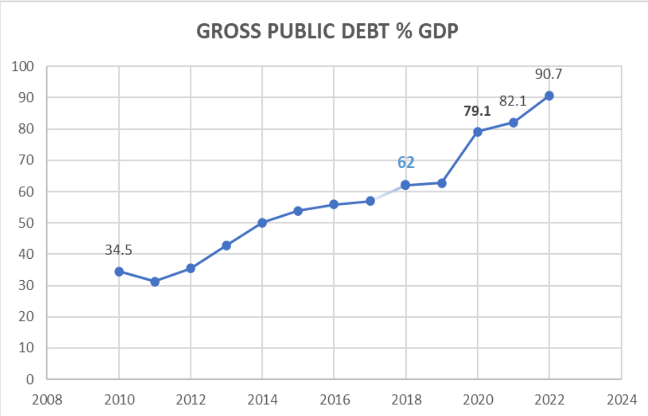

Figure 1

Additionally, Ghana surpassed both its stated goal of maintaining a debt to GDP ratio of 60 percent in 2018 and the IMF's recommended maximum debt-to-GDP ratio of 70 percent in 2020. *This is shown in the figure 1 above.*

Coupled with low domestic revenue mobilization, this unsustainable debt level has plunged the country into its worst fiscal or economic turmoil in decades. By the end of 2022, according to Ghana's Finance Minister, debt servicing[1] was absorbing more than half of the government's total revenue and up to 70% of tax revenues.

The Ghanaian finance ministry has stated that this crisis can be traced in part to the government's excessive spending because of the Covid-19 outbreak and others have linked it to the Russia-Ukraine war. Given that almost all countries in the world are affected by the pandemic and the war in Ukraine but with different economic outcomes, some are attributing economic challenges to improper management of the economy to mitigate external shocks.

But, are these the only causes? The Ghana cedis has in the last two years undergone significant depreciation against major foreign currencies, especially against the U.S dollar. In January 2022, one US dollar equaled Ghc6.2968, but by the end of 2022, the Ghana cedis had devalued by more than 100 percent, with one dollar equaling Ghc14.07. With more than 70% of Ghana's debt in the US dollar, depreciation of the cedi means higher debt service costs.

Debt Concessionality- Ghana's new private debt is less concessional. Ghana's high economic growth and economic status upgrade by global agencies like the World Bank has made it ineligible for concessional loans. That is not to say economic growth is bad or unhealthy, in fact that should be the country's goal. The argument is to highlight that Ghana's debt has now become more expensive. Even in the wake of a debt restructuring program, domestic debt servicing alone is projected to take up to 37% of the government's budgeted expenditure.

Downward Credit Rating- Fiscal imbalances have contributed to Ghana's declining credit rating, which was recently downgraded by S&P Global Ratings from B-/B to CCC+/C, putting the country's creditworthiness in jeopardy. With external investors holding up to 42% of total public debt, Ghana's external liquidity situation is very exposed to external private investor confidence and conduct. Low investors' confidence in Ghana's sovereign bonds and economy is leading to capital outflows, loss of external market access, and rising domestic borrowing costs according to the IMF report on Ghana's economic outlook in July 2022.

What are the Consequences? Ghana's debt sustainability analysis indicates that the country's debt is unsustainable. This means Ghana is unable to meet all its debt obligations, necessitating the need for a debt renegotiation programme. This is also required to secure an IMF programme to help strengthen the country's fragile fiscal balances.

Key Facts

Indebted countries are not poor, most of them are resource rich countries who, due to some domestic policy choices and especially external shocks have become cash strapped.

Debt accumulation has arisen largely because of the need to close the huge gaps in development financing that is required to achieve SDGs and in recent times because of the need to manage the emergent cost of living crisis because of the pandemic and the war in Ukraine.

Perception of high risk (problematic credit rating) associated with high investments in developing countries has reduced their capacity to access capital at a time when they need huge investment in economic and social infrastructure to drive structural transformation.

[1] Over 70% of tax revenues used for debt servicing - Ofori-Atta (citinewsroom.com)

Some Solutions

Illicit Financial Flows: Ghana decisively curbs trade related illicit financial flows through trade mis invoicing using digitalization and enhanced capacity of relevant institutions and cross-border collaboration as well as strong sanctions to punish defaulters. Through efficient systems and transparency, Ghana can strengthen its financial and regulatory systems and ensure openness and accountability. For example, through independent auditing of government taxation systems leveraging local and international mechanisms such as UNDP-OECDs Tax Inspectors Without Borders (TIWB).

Fiscal Consolidation: A robust fiscal consolidation that builds on the ambitious deficit target in the Fiscal Responsibility Law of 3-5% of GDP and the adjusted 2023 budget by providing a clear consolidation plan. This will help to build investor confidence in Ghana's economy and enhance access to external financial markets. Fiscal discipline combined with strong monetary policy will stabilize inflation, exchange rate and lower the cost of borrowing.

Domestic Resource Mobilization: Ghana finds innovative ways to capture internal revenues including digitalization and tapping into the large informal sector. Local authorities should continue to enhance capacities to mobilize internally generated revenue and the overdependence of Ghana's 261 MMDAs on central government transfers. These resources can be channeled to local economic development.

Comprehensive public financial management (PFM) reform noting that an effective PFM system requires the following:

1. Fiscal sustainability**:** avoid further debt
2. Allocate resources (for now, only to) strategic priorities
3. Ensure value for money in service delivery and
4. Foster transparency and accountability.

All these four should form critical part of the PFM reform agenda and should be undertaken simultaneously.

Some suggested global support for much needed development financing in developing countries.

• Global response should help unlock development financing through multilaterals and development banks to de-risk investment and encourage long term development financing from private capital in developing countries.

• Countries should be supported to focus economic growth on export driven growth, as they need to earn the foreign currency required for debt servicing.

• Increase concessionary funding over sovereign debt from private lenders.

• Developing countries urgently need support on capacity for debt management. This will entail careful management of opportunities, risks, and costs of debt; this is critical in avoiding a debt trap.

• Support to boost domestic revenue as an alternative to more borrowing is a worthy option to pursue in addition to increasing export led growth.

What will be the role of the United Nations in Ghana? Tight fiscal headroom means that Ghana's financial deficit in reaching the SDGs grows. The UN can however support in the following ways:

• **Support Ghana's Fiscal Consolidation Efforts-** The UN in Ghana, leveraging its global platform, can establish knowledge sharing mechanisms aimed at specific sectors such as public financial management and best practices in fiscal consolidation strategies.

• **Design and implement innovative financing initiatives** that unlocks the numerous untapped resources in Ghana including the diaspora and halting illicit financial flows. Examples of such initiatives include the UNDP led Integrated National Financing Framework, tapping into the novel carbon markets, green bonds/climate financing in general, among others.

• **Identify and support social sectors** that are deprived of critical social interventions, such as in education, health, etc. as a result of Ghana's unhealthy fiscal condition.

• **Strethening local systems and align public and private finance for the SDGs:** scale up UNDP's work that aims to direct private capital for SDGs invesment and ensure Ghana's socio-economic policies and tax administration increasingly aligns with the SDGs and address the different experiences, impact and needs of male and females.

What should private financial institutions and donors do to reduce the debt burden?

Looking outward in addition to domestic efforts for solution to the debt situation is important given the two main players of external debt.

Given the huge funding gap for meeting the SDGs and for mere survival in the middle of a lingering global pandemic and volatile global economy, many developing countries will continue to depend on foreign capital markets for development financing.

As a result, UNDP has produced evidence on the urgent need to **Reform Credit Rating System**. Credit ratings that provide (sometimes erroneous or inaccurate) information on credit worthiness of developing countries are increasingly important determinants of access to capital markets for these countries. Studies have shown that the credit rating system are clouded with inaccuracies and unfavorable credit ratings have been known to impede growth, with negative impacts on economic and political stability. Critics of the credit rating system have also recommended an African credit agency.

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