

Proceedings of Workshop on Economic Policy

May 4, 2001

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Sigma One Corporation

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Work Shop on Economic Policy, May 4, 2001

Dr. Kwame Apraku

(Minister of Trade and Industry)

Dr. Apraku, the Minister for Trade and Industry presented a paper on the State of the Ghanaian Economy with specific emphasis on economic policies that have been adopted by the country so far.

He begun his presentation by giving an overview of the state of the economy which he described as being weak. He proceeded to identify some critical issues that have to be addressed to enable the economy improve.

Budget Deficit:

The Budget Deficit was described as the most fundamental problem that the country had. Dr. Apraku stated that in 1997 the budget deficit had been 8.5% and a commitment was made to systematically reduce it every year so that by the year 2001, the country would have a balanced budget. However this did not materialise since now in 2001, the budget deficit is between 8.5% and 9%. This he said clearly showed that nothing had been done. Dr. Apraku further went on to say that it was important to deal with the budget deficit because the private sector is currently being starved of funds and Government's increasing borrowing would lead to a state of instability. He appealed to participants to focus on the budget deficit as the most fundamental problem in the country today and once it was addressed, the process of stabilising the economy would have begun. He appealed to participants to come up with practical, credible and achievable ideas that would help in reducing the budget deficit such that it would be eliminated by the year 2005. The reduction of the budget deficit, could not however be done in isolation but in line with monetary policy to ensure that everything else is covered.

Components of Fiscal Policy

i. Restructuring Tax Administrative Systems

Dr. Apraku said that the needed to be a fundamental overhaul of the tax administrative systems to reduce the corruption, tax avoidance and tax evasions. He also stated that requests for tax exemptions to his ministry were so many and measures had to be put in place to stop this practice since it had a negative effect on the economy of the country. He was of the view that revenue collection had to be improved. This he said could be done by putting an end to the corruption that occur at the destination inspection companies as a result of the collaboration between the companies ,importers and exporters. He reiterated the fact that there is a lot of money to be collected and urged participants identify creative ways by which the tax system of this country can be reformed.

ii. Restructuring Government

Dr. Apraku admitted that there were a lot of inefficiencies that exist within the Governmental machinery. He stated that the world had undergone some significant changes, since the establishment of the various government institutions and as such, the role of these institutions had to be redefined and a distinction made as to whether they are supposed to serve the private sector or the bureaucratic needs of Government. He further stated that, institutions that are designed to move the private sector forward need to be identified and their goals well defined to enable them accomplish it. Dr. Apraku said that Government was interested in a private sector oriented economy and this had to be reflected in the organisations and structures of government, budgetary allocations, policies and other programs. He also stated that there were certain agencies within the Government's structure that need to be abolished and their resources channelled into more productive areas that will advance the national agenda.

iii. Inflation

With regards to inflation, Dr. Apraku said that once a good monetary policy was in place, inflation could be dealt with and policies would be put in place to address it. He also stated that to achieve this there had to be good coordination between fiscal and monetary policies.

iv. Private Sector

Dr. Apraku stated that the private sector has not been successful over the years since no success has been achieved in any specific area. He said there was the need to identify about four key areas within which to excel so as to build confidence and arouse enthusiasm in the sector. The areas identified were:

- Agro – Processing
- Garment / Textile - Target the AGOA initiative
- Fish Processing and export – Greater investment in deep sea fishing
- Aluminium Products
- Agricultural Sector – Diversify sector by collaborating with other countries who are well established in this sector

v. Collaborating with other Ministries & decentralisation

Dr. Apraku stressed that there had to be collaboration between the various ministries specifically the Ministries of Women Affairs, Trade and Industry and Local Government.

He said this was because a large percentage of the country's population are in the rural areas and the bulk of small scale operators of the local industries in these areas are run by women. He further stated that success with the rural industries ultimately resulted in the success of export programmes.

Dr. Apraku further stressed that decentralisation is a mechanisms that could be put in place to help address the poverty situation in rural Ghana.

vi. Government Borrowing

Participants were urged to explore the possibility of setting a credit ceiling for Government borrowing.

DISCUSSION GROUP I

The State of The Ghanaian Economy (A Macroeconomic Perspective)

Paper by Dr. S. Ashong. (CEPA)

The paper presented gave an overview of the state of the Ghanaian economy and recommended specific fiscal measures and its implications.

The state of the Ghanaian economy was discussed under the following topics:

- The Fiscal Stance
- Monetary Developments
- External Sector Developments
- Domestic Debt

Dr. Ashong explained that various economic indicators at the end of the year 2000 portrayed an economy in dire straits. Weak macroeconomic fundamentals consequent upon an unsustainable combination of exchange rate, fiscal and monetary policies, created the basis for economic crises. A manifestation of the fragile macroeconomic fundamental is reflected in the acceleration in the rate of inflation, unbearably high nominal interest rates, and the emergence of large and persistence fiscal imbalance. The current account-induced balance of payments- triggered by the external terms of trade of trade difficulties of 1999- also intensified in 2000. In spite of the large depreciation of the cedi the long queues exchange from the banking systems that development in the third quarter of 1999 are yet to be eliminated. As a result the foreign exchange market is badly distorted and is being threatened by resurgence of the dreaded black market. Unemployment for both the skilled and unskilled in rising. Despite some improvements the level of poverty remains high and has deteriorated in some regions in the country. Interest payments on the national debt have become the largest single category of government spending programs this crowding out some pressing social demands on the budget.. He noted that this was not good for poverty alleviation and social stability of the nation given heterogeneous composition of our ethnic structure.,

Given the crucial importance of fiscal efficiency and discipline in improving macroeconomic fundamental, the following fiscal measures were recommended by S. Ashong which formed the basis of the workgroup discussions:

- Government revenues must be generated through real growth
- A sustainable revenue base must drive government expenditures. Foreign assistance must play a complementary role and not a substitute for domestic effort
- Divesture proceeds must be used exclusively to reduce the size of the domestic debt
- Need to identify cost-push pressures that contribute to inflation and manage them well. Such pressures include energy cost and exchange rate depreciation
- Interest payments on the national debt have become the largest single category of government spending programmes thus crowding out some other pressing social demands on the budget. This is not good for poverty alleviation and social stability of the nation given the heterogeneous composition of our ethnic structure
- Failure to reduce interest burden on the budget would mean some cutbacks or tax increases or both. Unfortunately, such cutbacks more often than not disproportionately disadvantage the poor while the chosen tax handles have also a higher incidence on the same group
- Efforts must be made to avoid any fiscal illusion. The practise whereby development expenditure is slashed to meet performance criteria targets often ignores quality issues. The composition of the expenditure of the expenditure both in terms of the sector mix and regional balance. More importantly, it only succeeds in reducing the country's future growth prospects while also increasing its reliance on foreign aid for development.
- Need to consolidate and formalise all arrear both by the central government for an orderly retirement plan of the domestic debt to be formulated.
- Proceeds from divesture sales should be used to primarily to retire the domestic debt, particularly those of short-term maturities. This will have the effect of reducing the interest burden on the budget in future years.

He also outlined certain pressing issues for 2001.

- A target of 5 percent real GDP growth is necessary, even though not sufficient, to have an impact on reducing poverty.
- Average inflation of 35% and a December year-on-year of 20% appear to be the only realistic and credible targets without compromising growth prospects.

These require M2+ money supply growth to be constrained to no more than 20 percent December year-on-year basis. The budget must also be programmed in such a way that domestic borrowing by the government is reduced to the barest minimum.

He noted that to achieve this the government would require about \$350 million in net external aid inflows of which \$300 million will be earmarked for budgetary support and \$50 million used to support the balance of payments.

Recommendations And Action Plans

1. IMPROVE RESOURCE MOBILIZATION

- Create a special bank account for Ghanaians in the Diaspora e.g. The Indian experience by January 2001. *(MOF / Parliament (Under certificate of emergency))*
- Critically examine and review import tax exemptions and reduce to barest minimum (Consider uniform tariff) by January 2002. *(MOF / Parliament)*
- Collecting Agencies (IRS, VAT, CEPS)
 - Decentralise revenue mobilisation by January, 2003 (MOF/Local Government)
 - Identify loop holes and plug them by June, 2001 *(MOF/Parliament)*
 - Regular auditing
 - Improve capacity
- Set realistic revenue targets by June 2001. *(IRS, VAT, CEPS, MOF)*
- Comprehensive special database system to enhance revenue collection e.g. national ID cards by January 2002. *(Local Govt)*
- Enhance property tax collection (Especially in urban areas)
 - Check whether property tax is being collected effectively

2. DOMESTIC DEBT MANAGEMENT

- Restructure debt instrument by short to medium term. *(MOF)*

- Divestiture Proceeds should be used exclusively to reduce domestic debt by September 2001. **(MOF/DIC)**
 - Identify what is left to be diversified
 - Identify what is owed already (audit arrears)
- Formalise the informal debt e.g. contractor payments (audit stock of payment arrears) by December 2001. **(MOF/BOG/MDA)**

3. EXPENDITURE (Examine expenditure profile)

- Finish all viable existing projects before new ones are embarked upon to realise the full benefits from them. **(MOF/Parliament)**
- Review procurement and contract system and come up with clear guidelines regarding procurements and awarding of contracts. **MOF/Parliament)**
- Reduce transportation expenditure
 - Parking lots at entry points into cities by 2003 – Medium term. **(Private Sector Participation)**
 - Government vehicles should not be used after working hours – proposed to take effect immediately. **(Chief of Staff/MOI)**

4. SET MACRO ECONOMIC PERFORMANCE TARGETS

- A December year-on-year inflation rate between 20 – 25% should be achieved in order not to compromise growth prospects. **(MOF/BOG)**
- Government should balance budget by 2004. **(MOF/BOG)**
- Real growth of at least 5% needs to be achieved to have an impact on reducing poverty. **(BOG/MOF)**

DISCUSSION GROUP II

Fiscal Discipline in Ghana

**Paper by
Dr. George Apenteng**

The workshop discussed fiscal discipline in Ghana using the paper presented by Dr. George Apenteng of the Institute of Economic Affairs as the basis for the discussion.

Dr. Apenteng postulated that the causes of increased fiscal vulnerability lies in the *loss of fiscal discipline of the government, which in turn can be attributed to*

rapidly rising government expenditure against the background of stagnating government revenue. He explained that government spending in nominal terms increased from fifteen billion cedis (¢15bn) in 1983 to nine thousand, nine hundred trillion cedis (¢9.9 trillion) in year 2000. In less than a decade, debt service payments have increased from 10% to account for 39.3% of the total government outlays in year 2000. His paper discussed fiscal issues under the following sub-topics:

- Tax Revenues
- Government Expenditure
- IRS, CEPS and VAT Secretariat
- Bonded Warehousing and Free Zones System
- Accessing Donor Inflows
- Expenditure Overruns
- Divestiture Receipts
- Local Government Assemblies
- Performance of Donor Funded Expenditure Control Projects, and
- The state of Government Accounts

The recommendations flowing from his paper centred on:

- Using divestiture proceeds for debt reduction and development
- Seeking donor support under HIPC to bridge financing gap
- Restructuring of Divestiture Implementation Committee
- Promotion of a spirit of transparency and accountability
- Raising of fuel prices to cost recovery levels
- Minimizing of unproductive government expenditures
- Harmonization of fiscal and monetary policy policies to curtail government borrowing to levels consistent with macro targets for second monetary zone.

The group then discussed the issues raised and considered them for analysis, prioritization and allocation of responsibility for improvement. Critical issues for fiscal discipline were then outlined as:

- Improved record keeping and monitoring of systems by the Ministry of Finance
- Placing a ceiling on Government Borrowing
- Regular reports on expenditure to be submitted to parliament by the Central Bank, and
- Strengthening the institutional capacity the Ministry of Finance to manage independent flow systems on accrual basis.

Based on the above, the group made recommendations to streamline and instill discipline into the country's financial management systems.

Recommendations and Action Plans

Recommendations for the improvement in fiscal discipline were made generally and specifically to cover expenditure, revenues and taxes, and attached responsibilities for the implementation of each recommendation to an appropriate sector ministry, department or agency.

General Recommendations

1. Record Keeping and Monitoring

This was further explained to mean the following:

- Stock taking of debts and arrears. (Ministry of Finance)
- Flow reporting system on expenditure (Controller and Accountant General)
- Transparency and control systems (MOF/BOG/Parliament/IMF/WorldBank)

2. Borrowing ceiling to be pre-agreed. Alterations to be made by parliamentary approval only (MOF/BOG/ Parliament)

3. Central bank to report to Parliament regularly on borrowing. (Parliament)

4. Institutional capacity of Ministry of Finance to be strengthened to implement and run an accrual basis reporting system. (MOF /MDAs)

Recommendations on Expenditure

1. Adoption of sectoral budgeting with defined output indicators and sectoral accountability sanctions (MOF/MDAs)

2. Decentralisation of sectoral Budget son a zero basis (MOF/MDAs)

This refers specifically to:

- Medium Term Framework
- Performance Incentives

3. Review the Divestiture process to make it transparent with respect to:

- Valuation of Assets
- Terms/ Timing of Payments
- Maintenance of Asset Value

Responsibility for this lies with Ministry of Finance and MDAs.

Recommendations on Revenues

- 1. All divestiture proceeds should go towards debt reduction (MOF/MOTI)*
- 2. Review the low base of non-tax income and fees revenue e.g District Assemblies, Police Service (MOF/Parliament)*

Recommendations on Tax

- 1. Close Tax loophole e.g duty exemption, customs bonds (MOF)*
- 2. Simplify customs duties e.g. 2 flat rates (MOF)*
- 3. Establish Tax Audit Authority to quantify national tax potential (MOF)*
- 4. Networking of Tax Agencies increase coordination and efficiency in tax collection (MOF/Proposed Tax Authority, IRS)*

DISCUSSION GROUP III

Macro-economic

Stabilization

Paper by Dr. Gockel

Ghana's economy was described as having multiple shades of macro-economic instability which were reflected largely in intractable inflation, persistent declining cedi-exchange rate and very high lending rates with large spreads. Hence these issues were selected to be the main focus of discussion in order to develop key recommendations.

Dr. Gockel indicated that analysis has shown that by its action Bank of Ghana is controlling two important prices, the exchange rate and interest rates, through its interventionist policies and that, although there is an argument in favour of using a fixed exchange rate commitment as a nominal anchor for an inflation-prone economy like Ghana, the exchange rate would still have a pro-equilibrium role for real targets, especially in response to adverse external shocks that call for a real depreciation that would not ordinarily be readily achieved through flexible domestic prices and wages.

Participants were asked to note that while arguments for a nominal foreign exchange anchor are appealing, the shocks that tend to disturb Ghana's economy are fundamentally external and environmental. The choice of a monetary target to manage inflation and other economic objectives would be more suitable than the exchange rate as a nominal anchor.

Generally, two things were said to be required for the effective conduct of open market operations:

- (i) Bank of Ghana must have control over its balance sheet and
- (ii) there must exist a good professional money market.

A lot of concern was expressed over some of government's institutions that tend to have unlimited access to funds from the banking system and consequently impact Bank of Ghana's balance sheet. These institutions, namely VRA, TOR, GNPC and ECG have acted independently to compound Government's fiscal deficits, especially as their debts were monetized by Bank of Ghana.

Another major concern was the lack of transparency in the open market operations of the Bank of Ghana. Participants felt that if the bank resolved to be more transparent, it would go a long way to ensure that the price of the instruments will reflect the market price, and subsequently, trading in secondary securities will also reflect changing market conditions, and attract capital gains or losses.

In making recommendations participants concluded that transition from a highly controlled economy to a market-oriented financial system is a very complicated process and would entail tenacity of purpose.

Recommendations and Action Plans

The workshop developed five crucial recommendations with corresponding action plans which they felt were critical to macro-economic stabilisation and were the responsibilities of the Ministry of Finance and the Bank of Ghana. These recommendations are stated in order of priority.

1. Reduce Government Deficit to 0% by 2005

Actions

- Establish an Act of parliament to regulate budget deficit and gov't borrowing
- Parastatals (e.g. VRA, ECG, GNPC and TOR) should not be allowed to borrow directly from Bank of Ghana

2. Enforce the independence of Bank of Ghana

Actions

- The number of Government appointees to the Board of BOG must be reduced
- Government must appoint more technocrats to the BOG Board
- Licensing & Liquidation of banking institutions should be the responsibility of BOG
- Level of government borrowing at BOG should be agreed upon every year at the beginning of the year
- The Governor of BOG should be the Exchange Controller and not the Minister of Finance

3. *Harmonize definition of ‘Money’ (M2+) with existing exchange control and Legal Tender regulations*

Action

- Banks should be allowed to keep reserves in the currency they mobilize.

4. *Increase transparency of BOG operations*

Action

- This should include OMO & Foreign exchange operations
- Establish an effective public affairs unit
- Disseminate information through publications and workshops

5. *Design and implement an orientation program for BOG staff and the banking industry*

Action

- The Programs should include
 - Training
 - Workshops
 - Publications

DISCUSSION GROUP IV

Environment, Science & Technology

Prof. Akwasi Ayensu

*Deputy Director-General
CSIR GH.*

The paper presented during the workshop emphasized on the fact that to raise the standard of living of the citizenry and to maintain vibrant and high performing economy, it is necessary to adopt Science & Technology as the basis of achieving sustainable development. Such an action will require constant review of policy issues and political commitment, management issues, funding and prioritization of research and development, standards, and benchmarking and regularity framework on the environment.

The presenter also touched on the fact that, environmental issues are pertinent to all aspects of economic development especially in infrastructure development, energy generation and agriculture.

Prof. Ayensu also explained that Environment, Science and Technology pervades all sectors of the economy (agriculture, health, education, energy, environment, trade, industry, natural resources, human settlements, transport, communication, etc.) Hence, the need for horizontal and vertical linkages to ensure cost-effectiveness in implementing programmes. Researches should be carried out from laboratory through pilot plant operations to production and

transfer of technology which requires a multidisciplinary approach for research results to be commercialized. E.g. Food processing – crop production, harvesting, storage, machinery, quality control and marketing – involves the following ministries: Finance, Environment, Science & Technology and Trade & Industry.

Recommendations and Action Plans:

1. ***Institute a new management structure for Science & Technology development (appreciation, funding, political commitment)***
 - Set up a new Apex body in the Office of the President (Best practice in all industrialising countries)
 - Improve linkages and coordination of Science & Technology activities
 - Institute programs for science acculturation in the citizenry

2. ***Develop comprehensive Techno-Economic Policy***
 - Government to identify Strategic Industries that can promote our export of manufactured products. e.g. Aluminum & vehicle parts
 - Develop skilled manpower for Science & Technology activities
 - Set up technology parks and incubation centres for innovation (non-project grants)

3. ***Building capacity for regulation and enforcement for restoration of degraded environment***
 - Training of manpower for environmental issues
 - Provide equipment and other resources to environmental agencies
 - Integrate environmental concern in all development programs
 - Ensure efficient natural resources management
 - Promote the setting up of recycling plants
 - Enforce environmental sanitation regulations

Ghana-Vision 2020

The Second Step

The long term goal of Ghana-Vision2020 is “to improve the social and economic status of all individuals and to eliminate extremes of deprivation by encouraging the creativity, enterprise and productivity of all citizens.”

Despite initial difficulties encountered in the effort to achieve middle income status within 25 years, ample evidence shows that the goal is attainable. The challenge for the next medium term plan, focuses on putting together the building blocks that would lead to structural transformation of the economy while reducing poverty significantly. The emphasis of rapid growth through accumulation and redistribution, as indicated in the Ghana Poverty Reduction Strategy, is maintained in the objectives and strategies for the policy framework

In the review of the development performance under the first step of the initiative the following issues were raised:

1. The enormous human capacity problems in the management of policy, structures and institutions that would lead to growth and development have become obvious
2. Economic reforms have not been pursued in a consistent manner.
3. The inability to attract foreign investment makes it significantly difficult to finance public and private sector planned activities.
4. There is little incentive and opportunity for research and technology development due to lack of new investments
5. The continuity of poverty and weak management has collapsed all safety nets , there by inhibiting meaningful contributions to national development by the poor.
6. The approach of decentralized administration has not had the expected impact on the problem of rural development due to enormous implementation omissions.

The key issues identified influenced the focus of government policy in the medium term in the following areas:

- Continuing Macroeconomic reforms
- Capacity-Building
- Development of Science and Technology Capacity for Production
- Developing Safety Nets for the Poor
- Ensuring the effectiveness of decentralization
- Achieving Public-Private Partnerships