Mark Evans

In the latter part of 2014 global oil prices fell at one of the most rapid paces in history. In Ghana this exposed a precarious fiscal situation that has undermined the high ambitions expressed by Ghanaians just a few years ago. Countries like Uganda and Tanzania that are currently shaping policies and laws to manage “resource curse” pressures can surely learn from Ghana’s troubling experience.

In Ghana, the story of the fall in oil prices cannot be separated from the fragility of the budget before the decline. In 2012, an election year not long after the start of oil production, civil service pay reforms and the introduction of a fuel subsidy triggered a rapid expansion in the budget deficit. This has since proved difficult to rein in.

By early 2014, just two years on from the conclusion of Ghana’s last IMF program and three years since oil revenues began flowing, government debt was again becoming unmanageable. To spur action to address the budget deficit, the government published a “homegrown” plan that ultimately directed conversations toward a return to the IMF. As the IMF noted at the time, Ghana’s public finances and economy had been left exposed. Then the oil price collapsed.

Ghana has tools to manage the impact of an oil price shock. Back in 2011, well aware of the hard-learned lessons of other oil producers, Ghanaian legislators passed the much-praised Petroleum Revenue Management Act (Act 815) (PRMA). This created the Ghana Stabilisation Fund, and accompanying fiscal rules that prompt saving when oil prices are high and cushion price falls’ impact on spending. These measures have recently been put to the test. The crash has not only tested this framework’s effectiveness in managing a price shock, but, combined with fiscal pressures, it has also tested the government’s willingness to adhere to the spirit of the rules. Initial results are not promising.

Facing financial difficulties, the government has made moves to unshackle itself from some of the fiscal rules. While the current situation may demand extraordinary measures, short-term solutions can easily undermine Ghana’s strategy for dealing with well-known problems associated with resource revenues. We have already started to see this.

The first example was in early 2014, when the government, already aware of the debt challenges ahead, took the controversial decision to cap the Ghana Stabilisation Fund. This allowed the government to use savings above a designated level and any future “excess” to manage the increasingly problematic budget deficit. By the end of 2014 over US $300 million had been removed from the fund, and projections of “excess” petroleum savings had become an integral part of government’s debt repayment plans. In the absence of detailed provisions for managing this process in the PRMA, this decision risked turning future petroleum revenues into a lifeline for an unsustainable fiscal deficit, and increased the budget’s overall vulnerability to an oil price fall. Ultimately, when the oil price did fall, there was a larger hole to manage than would have otherwise been the case.
In March 2015, the minister of finance hinted at a second and more definitive step away from the spirit of the Ghana’s petroleum revenue management laws. The minister suggested an upcoming revised 2015 budget would depart significantly from current stabilization rules and make painful spending cuts. This will be aided by amendments to the PRMA currently before parliament.

These current challenges do not stem from the fall in oil prices, nor specifically from weaknesses in the PRMA’s fiscal rules. It is worth noting that in 2015, petroleum revenues are supporting just 6 percent of spending. In the absence of broader budget problems and the decision to cap the stabilisation fund, Ghana’s fiscal rules could have cushioned the impact of the oil price fall on spending.

Ghana is some distance from the aspirations of five years ago. Domestically financed infrastructure spending as a proportion of total spending has almost halved since oil production began. Meanwhile, with debt increasing from about 40 percent of GDP in 2011 to close to 70 percent, interest payments jumped to over 25 percent of total spending in 2015. This is more than four times the spending financed by petroleum revenues. What has been given with one hand through petroleum revenues, has been taken by the other through decisions in the broader budget. Earmarking 70 percent of petroleum revenues for investment looks increasingly ineffective in this situation.

The country also now faces macroeconomic problems that look more like those of a traditional fiscal crisis, than a classic tale of the resource curse. Since 2013 the Ghanaian cedi has been collapsing at a painful rate, making it Africa’s worst performing currency in 2014 (and taking a bronze medal in the world rankings). Economic indicators such as interest rates, inflation and economic growth have also made for gloomy reading. This is not the economic transformation Ghana was looking for.

With decisions in the broader budget the source of these challenges, we now can see the consequence of focusing governance efforts primarily on petroleum revenues. Ghana has a history of election-year profligacy which, in 2012, was likely exacerbated by the prospect of future oil revenues. With hindsight we can see Ghana’s revenue management laws left an important gap by not addressing the issue of broader budget responsibility head on. This offers an important lesson for others.

In Ghana, few are under the illusion that meeting requirements in the IMF bailout program will be easy. 2016 will be another election year. In such an environment, using petroleum savings to help repay debt may become a political necessity. There may also be an economic case. Unfortunately Ghana’s fiscal rules do not offer a satisfactory mechanism for using petroleum revenues to ease current debt challenges. With such pressures, maintaining the integrity of Ghana’s strategy for petroleum revenue management will be a difficult project.

Mark Evans is an Africa economic analyst at the Natural Resource Governance Institute (NRGI).