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From shining success to deepening crisis

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Ghana, the second largest economy of West Africa and touted as an economic success is seeking assistance from International Monetary Fund for a bail out.

How did a prosperous nation with three major exports, gold, oil and cocoa happen to plunge into deep trouble?

What went wrong?

Ghana's economy

Ghana (population: 26 million; gross domestic product: US$47.9 billion; and per capita GDP: US$1,850) is a resource rich economy. Agriculture sector's contribution to GDP is 23 percent employing 42 percent of population; the manufacturing and industry accounts for 27 percent of GDP providing employment to 15 percent of population; and the services sector contributes 50 percent of GDP employing 43 percent of population.

Its newly emerging exports of digital technology goods and automotive and ship construction and traditional exports of gold and cocoa enabled Ghana to become the fastest growing economy in Africa and one of the top-ten fastest growing economies in the world.

Ghana is the world's second largest producer and exporter of cocoa, next to Ivory Coast. Ghana is also Africa's second largest exporter of gold next only to South Africa. Large discovery of oil reserves in 2007 and exports from 2010 brought prosperity.

Curse of oil

Newly acquired prosperity led the government to squander resources by resorting to populist programmes. For gaining support, salaries of civil servants and military were tripled during last four years. Salaries alone were 70 percent of tax income.

Fiscal deficits were above 10 percent of GDP. In 2013, revenue was 18 percent of GDP while spending was 28 percent of GDP. With revenues being stagnant as oil exports slowed down, government debt climbed to 56 percent of GDP.

Budget deficits and trade deficits are twins. The booming middle class began to consume luxury goods. Automatically, trade deficits swelled during last three years.

The current account deficits in the balance of payments also bulged in the context of other transfers such as remittances being unchanged. The growing balance of payments difficulties resulted in mounting pressures on exchange rate. The domestic currency, the cedi depreciated over last five years by 50 per cent. One cedi, the Ghanaian currency was equal to US 60 cents in 2010; today is just 27 cents, the depreciation being 56 percent.

As the depreciation of currency means higher import costs, inflation rose. In the basket of goods there is high import component. Further the cocoa farmers have to face higher costs of production as fertilizers and insecticides prices increased too.

Inflation in Ghana, as measured by the change in consumer price index, was 9.2 percent in 2012 as compared to 8.7 percent in 2011.

All too familiar?

What is happening in Ghana will remind every one of us in the Pacific region of the "lost decade" of the last century. The term, "lost decade" was used by a former governor of Papua New Guinea's central bank, when describing the boom-bust period of the 1990s.

The windfall gains in terms of high export earnings from mineral exports including petroleum and gas and non-mineral exports were squandered away by huge blow outs in terms of bonuses to civil servants and payouts to ministers and their cronies.

"In spite of high earnings from our mineral wealth and steady economic growth, because of gross fiscal mismanagement PNG was deprived of the opportunity to set the stage for progress and growth", said Governor Kami.

When the "bust" finally came, PNG was left in the lurch and it has to start all over again.

The lessons learnt were implemented in the later years.

It was decided to put the export earnings in trust accounts to be handled only by central bank, away from the control of the government.

Further, the central bank's autonomy was strengthened by the newly enacted Central Banking Act 2000, which safeguards monetary policy from any political interference and influence.

Back to Ghana

It is not the first time Ghana has gone to IMF.

It went to IMF in 2009 for a similar bail out for US$ 600 million when the emergency cash reserves were insufficient to cushion against a possible economic disaster. That was before oil exports which brought prosperity later.

In the latest May economic review of Ghana's economy, remedies were indicated.

Now with the formal application to IMF, they will be confirmed: cut the budget deficit now an additional two percentage points of GDP in 2014 alone, with more fiscal tightening needed in the years ahead.

IMF stands ready to help Ghana.

How about Ghana: ready to learn and act once for all against "fiscal abuse"?