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PROGRAM INFORMATION DOCUMENT (PID)

DRAFT Appraisal Stage: 18 October 2013
Report No.: AB7171
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Operation Name	Macro Stability for Competitiveness and Growth in Ghana
Region	AFRICA
Country	Ghana
Sector	Central government administration (44%); Oil and gas (25%); Transmission and Distribution of Electricity (13%); Other social services (12%); General finance sector (6%)
Operation ID	P133664
Lending Instrument	Development Policy Lending
Borrower(s)	THE GOVERNMENT OF GHANA
Implementing Agency	Ministry of Finance
Date PID Prepared	October 18, 2013
Estimated Date of Appraisal	October 31, 2013
Estimated Date of Board Approval	December 17, 2013
Corporate Review Decision	Following the corporate review, the decision was taken to proceed with the preparation of the operation.

I. Key development issues and rationale for Bank involvement

1.1 Ghana has registered significant progress in political and economic stability in the past decade and growth has accelerated as well. As a result, poverty decreased to 28.5 percent based on the last official figures. Growth has been supported mostly by positive terms of trade, cocoa and gold prices, and oil discoveries that sparked significant capital inflows. However, fiscal institutions need further strengthening to make policy more predictable and less volatile. Fiscal policy volatility directly decreases economic growth and, in addition, increases household consumption volatility. Given the concentration of households close to the poverty line (percentage of the population that is near-poor), volatility of fiscal outcomes leaves many households vulnerable to falling into poverty.

1.2 Enhancing government effectiveness is important for Ghana to become more competitive, which is essential to diversify its economic structure in order to mitigate the resource curse. Enhancing the productivity of public capital is also critical, because as Ghana transitions from IDA financing to market financing, the cost of funding will increase. Hence, the productivity of public projects will have to increase. The Bank has developed good knowledge of developing the economic institutions required to support this, namely the development of a public investment management system (PIMS) and the governance reforms required to make state-owned enterprises more efficient in delivering services.

II. Proposed Objective(s)

2.1 **The proposed Macroeconomic Stability for Competitiveness and Growth Credit is the first operation in a new programmatic series of three, following the poverty reduction operation series completed in 2012**. This new programmatic series aims to enable Ghana to address emerging challenges entailed by the transition to a resource-dependent middle-income country namely, the increased exposure to volatility and increased demand for public expenditure associated with the emergence of oil as an important new source of public revenues, and the rising cost of public funding as the country moves away gradually from concessional to non-concessional financing. These challenges call for institutions, programs and systems to retain a policy framework that will make policy more predictable, transparent and effective in delivering sustainable development outcomes.

2.2 **The objective of this programmatic series is to (i) support economic and fiscal institution reforms to reduce the volatility of fiscal policy outcomes; and (ii) increase the efficiency of public spending and service delivery**. The operation supports the government's development objectives set out in the Ghana Shared Growth and Development Agenda (GSGDA) for 2010-2013. The GSGDA emphasizes the need for macroeconomic stabilization and greater executive efficiency, transparency and accountability to provide an adequate setting for the reduction of poverty and socio-economic inequalities through agricultural, private sector, infrastructure and human resource development.

III. Preliminary Description

3.1 **The proposed operation supports the authorities' program of building a policy framework that will enable Ghana to confront the challenges entailed by the transition to a resource-dependent middle-income country**. One key challenge is the increased exposure to international volatility and increased demands for public expenditure resulting from the emergence of oil as an important source of fiscal revenue in addition to cocoa and gold. Policy should not be pro-cyclical as this tends to exacerbate volatility and damage fiscal sustainability. Policy volatility directly decreases economic growth and in addition increases household consumption volatility which, given the concentration of households around the poverty line, presents the risk that many households will fall into poverty, reversing the progress made in poverty reduction in recent years. Another critical challenge is the expected increase in the cost of capital as the country transitions from concessional to non-concessional financing. This underscores the importance of ensuring that policies, programs and mechanisms are in place to increase the productivity of public spending and enable the increased revenues from the natural resource sector to be used effectively for public service delivery. To help address these challenges, two broad policy areas have been identified.

3.2 **Component 1: *strengthening fiscal institutions to reduce volatility of fiscal outcomes.*** With oil emerging as a new important source of domestic revenue, the policy framework has to be such that it compensates for the additional volatility arising from various sources, including shocks to commodity prices and expenditure booms and busts originating from the political business cycle. A fiscal institutional framework that promotes predictable, credible and transparent fiscal policies is needed to reduce volatility in fiscal policy outcomes and help maintain macroeconomic stability.

3.3 Under component one the proposed prior actions are:

- Policy statement issued (i) linking the primary fiscal balance in the Medium Term Fiscal Framework to the Public Debt Target (as specified in the Medium Term Public Debt Management Strategy) and (ii) on adherence to WAMZ fiscal convergence criteria relating to the wage bill with a specified time horizon.
- Debt management reform plan issued by Ministry of Finance.
- Ministry of Finance to draft guidelines for undertaking credit risk assessments prior to the issuance of loan guarantees, on-lending, and other debt related transactions
- Publish public debt bulletin and data via reports and semi-annual publication of debt statistical bulletin on Ministry of Finance website.

3.4 **Component 2: *Enhancing the productivity of public spending and providing better public services*.** Achieving this objective requires reforms in a number of critical areas. First, *governance reforms of state-owned enterprises* must take place to reduce technical and operational inefficiencies to create fiscal space to fund increased investment spending, improve service reliability for the private sector, and enhance service levels for consumers. Second, improving the efficiency and viability of the *energy sector*. Third, *public financial management reforms* must take place to enable the public sector to plan, allocate, manage and report on public finances in a situation where public resources are expected to grow significantly. Fourth, improved *public investment management* is needed to enable the country to select the best public investment projects and implement them effectively. Fifth, there is a need to *enhance social protection*, whilst we transition to a targeted subsidy system.

3.5 Under component one the proposed prior actions are:

- Terms of Reference issued by Ministry of Finance for performance and governance assessment of SOEs including ECG, VRA, GNPC, GWCL.
- Terms of Reference issued by MoF for performance and governance assessment of regulators including BoG, NPRA, PURC, NIC, and SEC, by independent institution.
- GoG publishes an energy sector arrears clearance plan indicating the (1) baseline value (2) how and when they would be cleared and (3) how to avoid reoccurrence.
- Ministry of Finance pays VRA short-term debt originated in crude oil purchases as of June 2013, as part of debt refinancing plan.
- Electricity prices adjusted by 75 percent to reduce the gap between consumer prices and cost recovery level).
- GoG reduces to one third the subsidy rate on prices of gasoline, diesel, and LPG.
- An Agency Agreement is signed by October 30, 2013, between the BoG and the MoF that all GoG bank accounts, regardless of fund type, held at the BoG (Accra) and 5 BoG branches (Kumasi, Takoradi, Sunyani, Hohoe, and Tamale) be linked through Treasury Single Account (TSA) for cash management.
- Public Investment Management (PIM) Strengthening Action Plan approved by Cabinet.
- Ministry of Finance releases budgetary resources to MoGCSP for all outstanding LEAP payments up to April, 2013.

IV. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

4.1 **Measures supported by the proposed operation are expected to have a positive and direct impact on poverty reduction**. These include: (i) improving subsidy targeting and execution of LEAP payments to provide more social protection to the poor; (ii) strengthening PIM for improved allocative and operational efficiency of public expenditure; and (iii) restoring the financial viability of the electricity sector, which is critical for pro-poor economic growth and job creation. More broadly, the proposed operation will support the macroeconomic stabilization program, and in doing so reduce the exposure of the poor and the near poor to macroeconomic shocks.

4.2 **A preliminary poverty and social impact analysis of the fuel subsidy reduction has been conducted**. It shows that, in the absence of compensatory policies, the reduction in fuel subsidies could have a short term substantial impact on poverty. A large number of people fall below the poverty line and the severity of poverty deepens for individuals already living in poverty. In terms of regional effects, simulations show that it is the more developed Southern and Central regions, being more urbanized, that are more affected by the price shock than the more rural and poorer Upper east and North. PSIA simulations show that increasing the size of the LEAP program can moderate the negative effects of fuel price increases on the poor. Many more than the existing 80,000 households could be accessed at a cost of less than the previous subsidies, especially if the LEAP can be made more accurate in targeting the neediest. In the medium term, however, the balancing of fiscal accounts is expected to contribute to macroeconomic stabilization and growth, necessary elements for job creation and poverty reduction.

Environmental Aspects

4.3 **Measures supported by the proposed operation are not expected to have any significant adverse impact on the environment.** The implementation of measures to: improve the governance of SOEs, strengthen PFM (including commitment controls), lay the foundations of a public investment management system, are each likely to be environmentally neutral. In the long-run improvements in sector planning, budgeting and financial management may have positive environmental impacts through more reliable and predictable financing for the ministries and line agencies in charge of managing natural resources and the environment.

4.4 **The adoption of the electricity automatic tariff adjustment mechanism has the potential to improve energy conservation.** Largely through the provision of clear market signals to consumers on energy's true cost. Furthermore it is not expected to induce any significant switching to dirty energy in net terms. In Ghana, electricity is used for lighting and running appliances, but not for cooking (which is essentially supplied by fuel wood), as reported in the various GLSSs. As such, electricity tariff increases could only induce switching to kerosene for lighting, but such a substitution effect is expected to be negligible given that poor households (typically the most sensitive to changes in relative prices of energy given its importance in overall budget) will not be affected. Besides, a greater use of kerosene would be offset by a lower use of crude oil to generate electricity. At the same time the establishment of a petroleum regulatory authority will help strengthen to Ghana's environmental legal and institutional framework and assist mainstreaming of environmental concerns in the emerging oil industry.

4.5 **The assessment of environmental and social risks (including from oil and gas) builds on Ghana's earlier efforts to comprehend the impact of development policy, so as to develop corresponding preventive and mitigation/remediation plans**. The Strategic Environmental Assessment (SEA) was introduced in 2004 as a process tool to evaluate the potential environmental (natural resources management linkage), social (poverty indicators, livelihoods and health impacts and vulnerability impacts on the poor) and institutional (institutional targeted impacts) effects of the Ghana Poverty Reduction Strategy (and successors) and any plans or programs that may be derived. A similar exercise is recommended for the latter phases of the proposed DPO series.

V. Tentative financing

Source:		($m.)
BORROWER/RECIPIENT		0
International Development Association (IDA)		150
Borrower/Recipient		
IBRD		
Others (specifiy)		
	Total	150

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