REPUBLIC OF GHANA

MINISTRY OF FINANCE

MEDIUM-TERM DEBT MANAGEMENT STRATEGY
2015-2017

APPROVED BY:

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MINISTER FOR FINANCE

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The Medium Term Debt Management Strategy 2015-2017 is also available at the Ministry of Finance Website at: http://www.mofep.gov.gh

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FOREWORD

His Excellency the President John Dramani Mahama has reiterated his commitment to ensuring macroeconomic stability and a shared growth for all Ghanaians in the medium term. To operationalize this broad policy objective, a number of economic instruments and strategies are to be adopted for the period. One of these strategies is our Medium Term Debt Managament Strategy (MTDS). The MTDS is a useful public debt management tool that recognizes the cost and risk trade-offs in setting sustainable borrowing limits and ensuring that debt is serviced under a wide range of shocks without risk of default.

Ghana's 2015 MTDS has been carefully drafted by taking into consideration the medium term macroeconomic fiscal framework, which among others covers prudent revenue projections and planned expenditures.

Being the third annual publication, the 2015 MTDS has been prepared to guide financing of the budget deficit. As indicated in the 2015 Budget Statement and Economic Policy of Government, the expected budget deficit is 7.5 per cent of GDP in 2015. It is for this important reason that this strategy does not only address the appropriate mix between domestic and external debt, but also defines the terms and conditions for new borrowing within the global economic environment.

Government is committed and will continue to take remarkable steps towards improving public debt management in Ghana. It is in the light of this that we are reviewing the 1970 Loans Act as part of our review of the public financial management laws. The new public debt law is expected to include a wide range of financial instruments, including financial derivatives. Currently, debt portfolio management has been facilitated through a reliable and accurate recording of public debt and close monitoring of the debt sustainability indicators.

Finally, permit me to state that Government is committed to achieving better development outcomes through improved transparency and accountability in public financial management. I see the publication of this Medium Term Debt Management Strategy report as meeting this commitment.

Going forward, we will ensure that we integrate this process effectively in our budget cycle, and the entire public finanacial management reforms.

It is my wish that this strategy paper is seen as a critical tool for informed policy decisions by all stakeholders, reducing the debt burden and other fiscal vulnerabilities and also serve to deepen relations with existing and potential investors.

Hon. Seth E. Terkper
Minister for Finance

ACKNOWLEDGEMENT

The MTDS tool seeks to analyse the cost and risk of alternative borrowing strategies. This Medium Term Debt Management Strategy (MTDS) as prepared by the Ministry of Finance outlines Government's plan to guide debt management operations over the medium term, 2015-2017. The strategy also seeks to deepen the domestic debt market by lengthening the maturity profile and at the same time ensures efficient access into the International Capital Market (ICM).

In the face of a dwindling access to concessional external financing, Ghana (middle income oil producing country) is re-strategizing to take advantage of available concessional resources for social projects while considering borrowing on non-concessional/commercial terms for infrastructure projects which are self-financing, as a means to minimizing costs and refinancing risks.

To this end, the 2015 MTDS plans to extend the maturity profile of domestic debt by issuing treasury bonds which will be biased towards the medium to long tenors to create benchmark bonds.

As you will find in this strategy document, the preparation and implementation of a MTDS is a technical exercise which requires highly skilled human resource capacity to undertake. I wish to at this point acknowledge all who contributed diversely to bringing this document into reality.

It is refreshing to note that the preparation of the 2015 MTDS document was spearheaded by the joint mission from the International Monetary Fund (IMF), World Bank and the West African Institute for Financial & Economic Management (WAIFEM), staff of the Debt Management Division of this Ministry with the support of Hon. Seth E. Terkper, Minister, his Deputy Ministers and Special Advisors.

The Ministry also recognises the contribution of officers from the Bank of Ghana, Controller and Accountant General's Department, and officers from the Economic Research and Forecasting, Real Sector, Public Investment, Budget and the External Resource Mobilization (Bilateral and Multilateral) divisions of the MOF. The Ministry appreciates the contribution of its staff and is particularly grateful to the core team including Eriko Togo and Tsayoshi Sasaki (IMF), Abha Prasad, Sayyora Umarova and Tobias Haque (World Bank), Baba Musa and Karamo Jawara (WAIFEM), Samuel Danquah Arkhurst, (Ag. Director, Debt Management Division), Yaa Asantewa Asante (Head, Investor Relations Unit), Dr. Zakaria Issahaku (Head, Strategy, Policy & Risk Management Unit), Ralph J.A. Ayiku, Doris A. Dzidzornu, Henry Kyeremeh, Dr. Mawuli Gaddah and all staff of the Debt Management Division.

Major (Rtd.) M. S. Tara
Chief Director
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SECTION 1: INTRODUCTION

1. Given the limited resource available to meet the development aspirations of a country, Governments usually resort to debt financing from domestic and external sources in order to undertake development projects and programmes. Debt may be an impetus for economic growth if borrowing proceeds are used judiciously in driving infrastructural development required for sustained economic progress. High levels of public debt may stifle economic growth if there is no strategy in place to contain heavy debt service burden. Having prudent debt management strategy therefore, ensures that right choices among several financing options are made while keeping in view cost and risk trade-offs. In the case of Ghana, the Loans Act, 1970, the 1992 Constitution of the Republic of Ghana, the Financial Administration Act 2003 (Act 654), the Financial Administration Regulations 2004 (LI 1802), the Public Procurement Act and the Bank of Ghana (BoG) Act, 2002 clearly provide the mandate of debt management in the country.

2. In this regard, the Government of Ghana has developed its Medium-Term Debt Management Strategy (MTDS, 2015-2017)[1] to ensure that the financing requirements are met at the lowest possible cost with prudent degree of risk and to develop the domestic debt market.

3. The MTDS seeks to provide more cost-efficient access to the international and domestic capital markets to meet Government's development needs. The essence of the MTDS primarily focuses on determining the appropriate composition of the debt portfolio, taking into account the macroeconomic framework and the market environment. The MTDS provides guidance on the appropriate mix of financing from different sources in the context of the trade-off between cost minimization and financial risk reduction.

Objectives and scope

4. The government's debt management objectives are to:
    - raise the required amount of funding to meet government's financing needs at a reasonable cost and subject to prudent levels of risk;
    - promote the development of efficient primary and secondary domestic securities markets; and
    - meet any other public debt management goals that government may have set.

5. The above stated objectives are in line with National Medium Term Development Policy Framework (Ghana Shared Growth and Development Agenda II-GSGDA).

6. The time horizon of the analysis is the medium term, spanning three years from 2015 through 2017. The scope of the MTDS 2015-2017 analysis is all central government debt with direct repayment obligation.

7. This strategy was prepared by the public sector stakeholders in debt management and has benefited from contribution from other external stakeholders.

[1] The Medium-Term Debt Management Strategy is a plan that Government intends to implement over the medium-term in order to achieve a desired composition of the Government debt composition, which captures the Government's preferences with regards to the cost-risk trade-off.

8. This strategy is structured as follows: Following this introductory section, Section 2 outlines the recent macroeconomic developments and Section 3 presents succinctly the cost and risk of the Debt Portfolio; Section 4 describes the borrowing strategy over the medium term; current debt management policies which are on-going and would support the strategy are presented in Section 5; and the conclusion is in Section 6.

SECTION 2: RECENT MACROECONOMIC DEVELOPMENTS

9. Recent price declines in Ghana's major export commodities coupled with domestic factors led to fiscal slippages during the past few years that rendered the debt management terrain difficult and reduced the effectiveness of policy responses to meet the desired target. The result was an increase in the borrowing requirement that was financed by the available external and domestic financing. With its resulting inflationary pressures and uncertainty, yields on domestic instruments rose, and posed a challenge for the existing debt management strategy which was to reduce the refinancing risk of Ghana's debt.

10. Debt management in the past had been a residual policy. Going forward, debt management policy is being primed to be an integral part of the overall macroeconomic policy framework to ensure consistency. The Medium-term Debt Management Strategy (MTDS) is a plan that helps to operationalize this objective through the choice of financing sources and instruments that balance the desired financing mix consistent with the macroeconomic framework, while making trade-offs on the costs and risks of these choices.

11. The macro-fiscal framework envisages a revised budget deficit of 7.5 per cent in 2015. The overall budget deficit position is to some extent influenced by the size of interest payments arising from the stock of existing debt. Containing the interest payment bill will be necessary to restore a sustainable fiscal balance, build market confidence, reduce the rate of domestic currency depreciation and anchor inflation expectation, and ultimately bring down domestic nominal and real interest rates. This will help to reverse the upward trend in public debt dynamics and reduce the risk of debt distress.

SECTION 3: DEBT PORTFOLIO REVIEW

12. The Government of Ghana has developed its MTDS to ensure that the financing requirements are met at the lowest possible cost with prudent degree of risk and to develop the domestic debt market. The MTDS primarily focuses on determining the appropriate composition of the debt portfolio, taking into account the macro-fiscal framework and the market environment in the most cost efficient way.

13. The MTDS analysis reveals a high cost of debt in Ghana. The weighted average interest rate of the total debt portfolio is about 11 percent. The high interest rates have been driven by several factors, including the recent depreciation of the local currency, larger rollover needs and a relatively high inflation. In the medium term, the average interest rate on external debt is likely to increase as Ghana gradually transitions toward less concessional borrowing. It is, however, anticipated that average interest rate on domestic debt will reduce over time as inflation would be curtailed through fiscal consolidation as outlined in the 'Home Grown' policies and the IMF programme.

14. The debt portfolio tends to have a high refinancing, interest and exchange rate risks. The refinancing risk is revealed by the fact that about 25 percent of the entire debt portfolio matures within a year, which represents about 16 percent of GDP.

15. A significant proportion of the debt portfolio is subject to regular interest rate resetting (re-fixing), which poses a risk in terms of budgeting for interest payments. About 35 percent of the entire debt portfolio faces different interest rates on due dates.

16. Fluctuation in exchange rates also poses a risk in managing the debt portfolio. About 56 percent of the debt portfolio is external, 65% of which is denominated in United States Dollars (USD).

SECTION 4: DEBT MANAGEMENT STRATEGY

17. Government intends to diversify its funding sources and lengthen the maturity profile of the debt portfolio. Government intends to issue a Eurobond in 2015, proceeds of which will be used to finance the buy-back of the 2017 Eurobond, maturing domestic debt and capital expenditure. The plan is to take steps to induce increased participation in domestic debt markets by resident and non-resident investors, including a possible opening of the 2-year bonds to non-resident investors. The strategy is based on the assumption that non-resident investors are expected to roll over their holdings of government bonds. It also envisages issuing inflation-linked bonds in 2017 targeted at pension funds and insurance companies.

Foreign Currency Risk Benchmark

18. In external debt portfolio, a strategic benchmark of 65 percent +/-5 percent exposure to the US Dollar is pursued. This is premised on the fact that a significant proportion of Ghana's international reserves and export receipts are denominated in US Dollars.

Interest Rate Risk Benchmark

19. The current structure of interest rate does not suggest any eminent interest rate risk for the debt portfolio. Over the medium term, the share of the floating rate debt in total external debt is expected to be within the range of 20 - 25 percent. The share of the entire debt portfolio facing interest rate resetting in a year is not expected to be more than 35 percent.

Re-Financing Risk Benchmark

20. The management of refinancing risk is pursued to avoid bunching of debt service obligations and/or rollover risk, which may lead to liquidity crisis and/or excessive increase in the cost of debt servicing. With this strategy, bullet repayment structure and accumulation of debt servicing in one period (especially the short dated domestic debt) will be smoothened to ensure that it is aligned with flows on revenue structure to avoid liquidity crisis and high re-financing cost. The share of debt maturing in one year is expected to be within the range of 20-25 percent. The Average Time to Maturity (ATM) of the debt portfolio is expected to be not less than 6.5 years.

SECTION 5: DEBT MANAGEMENT POLICIES

21. As part of the above stated strategy, and in support of Government's commitment to maintain sustainable debt levels, the implementation of critical debt management policies which were outlined in the 2015 Budget Statement and Economic Policy have already commenced. These are:

Concessional loans and grants

22. Government is committed in channelling concessional loans and grants to financing social infrastructure and non-concessional financing to self-financing capital projects

Implementation of the 'Golden Rule'

23. The Government intends to finance capital expenditure with long-term debt whilst using short term bills for liquidity management

Implementation of the On Lending and Escrow Arrangement

24. Government has a policy to on-lend proceeds of financing agreements, any related counterpart funding and other relevant financing costs to State Owned Enterprises (SOEs) and Metropolitan Municipals and District Assemblies (MMDAs). To ensure recovery of on-lent loans for commercially viable projects undertaken by SOEs, government has introduced an on-lending and escrow account initiative to minimize the impact of loans on the public debt portfolio.

25. By this arrangement, SOEs are required to open escrow accounts with any universal commercial bank approved by the Ministry of Finance where proceeds from the projects shall be transferred into. SOEs are required to open an account each in the appropriate currencies for all on-lent facilities.

Setting up the Sinking Fund

26. The objective of establishing the Sinking Fund is to manage the orderly redemption of Eurobonds and other debt instruments.

27. In 2015, 50 percent of the amount over the cap on the Ghana Stabilization Fund (GSF) will be paid into the Sinking Fund to build up resources to repay specified debt obligations of the government.

Establishment of the Ghana Infrastructure and Investment Fund (GIIF)

28. The GIIF was established by the Ghana Infrastructure and Investment Fund Act 2014 (Act 877). The fund is to mobilize, manage, coordinate and provide financial resources for investment in infrastructure projects. The establishment of the Fund will also enable self-financing projects to be taken off the government's debt stock and managed as commercial projects.

SECTION 6: CONCLUSION

29. With the coming into force of the MTDS for the period 2015-2017, the approved MTDS for the period 2012-14 has been annulled.