Ghana won’t be able to fix its economy if it uses last decade’s rule book

blogs.lse.ac.uk/businessreview/2017/01/25/ghana-wont-be-able-to-fix-its-economy-if-it-uses-last-decades-rule-book/

1/25/2017

Ghana’s 2008 general election remains one for the history books. The electorate voted out a government (the New Patriotic Party) that had presided over:

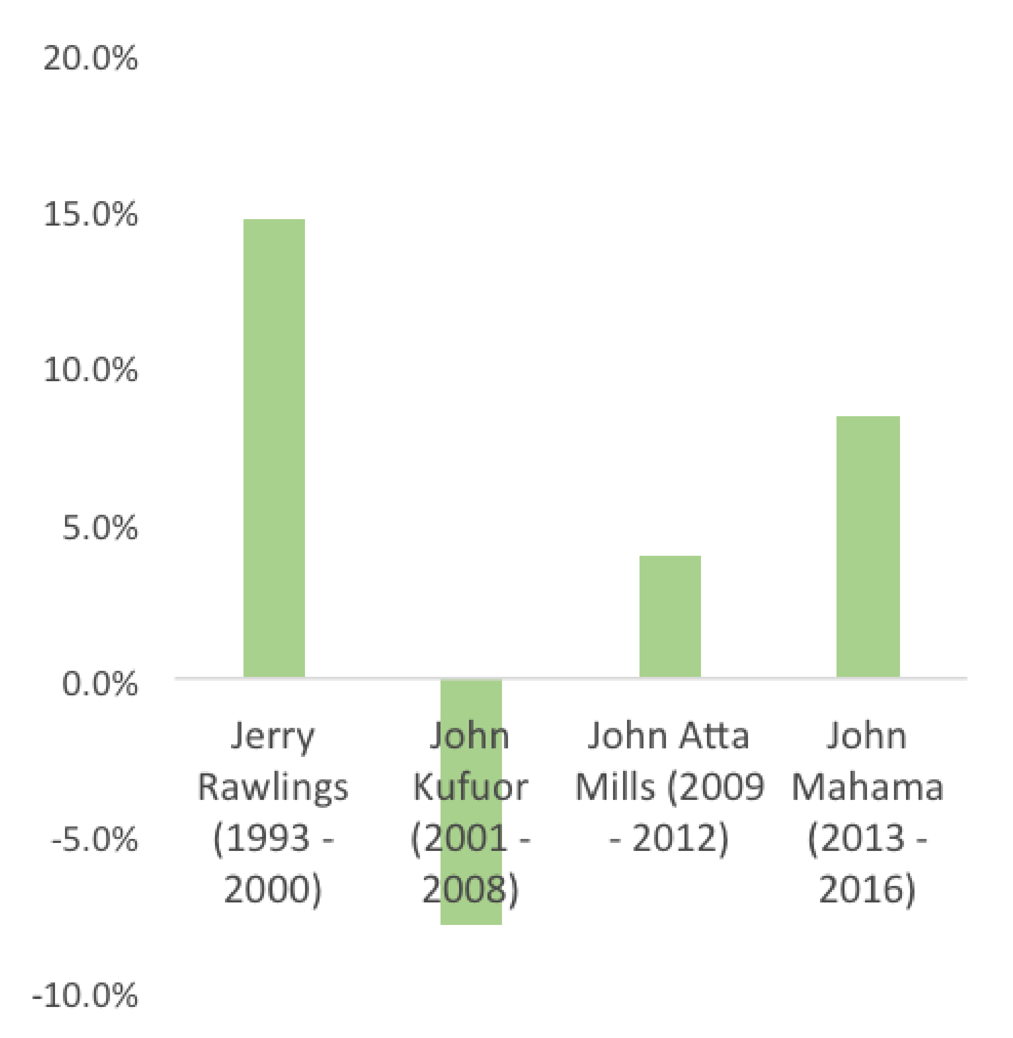
- a decline in the number of the unemployed masses (averaging a 7.9 per cent year-on-year fall in the number of unemployed between 2001 and 2008);
- a more stable monetary environment with a decline in annual inflation from 32.9 per cent in 2001 to 16.5 per cent in 2008 on the back of decelerated growth in money supply from the highs witnessed between 1993 and 2000
- a decline in imports as a proportion of the Gross Domestic Product (from 64.8 per cent in 2001 to 44.5 per cent in 2008);
- labour productivity that grew faster than during the preceding administration (2.9 per cent per annum versus 1.1 per cent), and
- a reduction in the average time required to start a business by 47.6 per cent between 2003 and 2008 to 11 days.

This is not to suggest that the New Patriotic Party (NPP) presided over a golden age for Ghana’s economy, not at all. In fact, pervasive allegations of a lacklustre fight against corruption could well have cost NPP the re-election in 2008.

It says, however, that eight years later, with a macroeconomic environment that is less than flattering and growth engines in dire need of rebooting (following the precipitous plunge in commodity prices and paralysis from the energy crisis), it should not be surprising that NPP won the presidency last year with the most decisive victory since 2004.

In President Nana Akufo-Addo's inaugural speech, however, he seemed to be reading from the old NPP rule book and the question that begs is whether it can deliver within a new set of circumstances.

Figure 1. Average yearly change in unemployment



Source: International Labour Organisation, World Bank

Figure 2. Imports as a percentage of GDP

Source: International Labour Organisation, World Bank

Why the pledge on tax cuts could be difficult to keep

One of the key take-homes from the speech was the pledge to reduce taxes in a bid to restore the economy's growth momentum. This pledge is important for two reasons:

One, it felt starkly reminiscent of the raft of tax cuts under former President John Kufuor's administration, including the reduction of corporate tax from 32.5 per cent to 28.0 per cent and withholding tax from 7.5 per cent to 5.0 per cent in 2005, and could imply the NPP economic rule book has not changed much since the last time it was in power.

Two, and more consequentially, the economy might not have the fiscal space requisite for supporting tax cuts in an environment where subdued commodity prices have depressed government revenue. The economy is under strain from a ballooning debt (the government debt to GDP ratio stands at 66 per cent against sub-Saharan Africa's average of 41.1 per cent, whilst between 2010 and 2014 the stock of domestic debt grew four-fold to $8.2 billion, according to the IMF).

Unless the wider policy mix undertakes accompanying slashes in government spending, the economy could be skating on thin ice with a budget balance that could roil further into deficit if it engages in an exercise of lone ranging with tax cuts. What's more? The NPP Manifesto is ambitious in expenditure and tax cuts could have the net effect of necessitating high deficit financing of government expenditure over the next four years.

The general tone in the second review of the Ghanaian economy under International Monetary Fund's Extended Credit Facility is one of greater need for higher revenue and proposes measures such as reduction in tax exemptions with a view to realizing this target.

The counter argument to this view is that the new administration could be banking on the possibility that tax cuts will rev up the economy and private sector enough to offset losses in revenue. Whereas this hope might not be unfounded, the timing of the same threatens to derail efforts aimed at strengthening the economy's fiscal position and mitigation of vulnerability to pressures from rising debt.

♣♣♣

Notes:

- *The data in the first paragraph, on inflation, imports as a percentage of GDP and duration taken to start a business are sourced from World Bank Development Indicators.*
- *The post gives the views of its authors, not the position of LSE Business Review or the London School of Economics.*
- *Featured image credit: Accra market, by Francisco Anzola, under a CC-BY-2.0 licence*
- *Before commenting, please read our Comment Policy.*

Julians Amboko is a Research Analyst with StratLink Africa Ltd, a Nairobi-based financial advisory firm focusing on emerging and frontier markets. He covers macroeconomic research and analysis for Sub-Saharan Africa, including markets such as Nigeria, Kenya, Ethiopia, Ghana, and Angola. He tweets at @AmbokoJH