Why does the IMF include the debt of state-owned enterprises in Ghana's public debt?

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The IMF, in its debt sustainability analysis, includes the debt of Ghana's state-owned enterprises (SOEs). The government of Ghana, prior to asking the IMF for support in July 2022, had excluded the debt of SOEs from public debt primarily on the grounds that such debt was not backed by the sovereign guarantees and/or were held by special purpose vehicles like ESLA Plc. This fiscal logic was evident in a response by the government to the NDC in November 2017. The NDC had claimed that ESLA bonds should be part of government debt. A part of the government's response was that the "… claim that ESLA is government revenue and that an ESLA backed bond must be treated as sovereign debt is incorrect. ESLA proceeds do not commingle with the consolidated fund and thus, cannot be treated as government revenue affecting GoG fiscals. **An E.S.L.A backed bond can equally not be treated as government/sovereign debt**." (https://mofep.gov.gh/press-release/2017-11-10/response-to-the-ndc%E2%80%99s-press-statement-on-the-esla-backed-energy-bond#:~:text=In%20all%20E.S.L.A).[1]

In a staff report dated November 21, 2019 (after the completion of the 2015-2019 IMF program), the IMF warned that "Off-budget operations, including ESLA, Sinohydro, and GETFund, contribute to public debt but their ***decentralized*** and not always transparent nature complicates oversight and management of public financing, raising the scope for corruption."

Eventually, the government acknowledged that the debt of SOEs (including special purpose vehicles) was part of public debt because the bonds (debt) issued by Daakye Plc (to finance education via GetFund), ESLA Plc (to pay for debts of the energy sector Levy, and Cocobod bills were included in the domestic debt exchange program. In his budget speech on November 24, 2022, the minister of finance, Ken Ofori-Atta said that "The Public Debt-to-GDP ratio stood at 75.9 percent at the end of September 2022." But twelve days later, on December 5, 2022, minister of finance, said that "… our total public debt stock, ***including that of State-Owned Enterprises and all***, exceeds 100% of our GDP. This is why we are today announcing the debt exchange which will help in restoring our capacity to service debt." Ghana's debt-to-GDP ratio increased from 75.9% to over 100% within twelve days or within two months (end of September 2022 to about end of November 2022) partly because of the inclusion of the debt of SOEs in public debt.

[1]In its response, the government exposed the NDC's double standard by noting that "It is also unbelievable how the Minority would want this debt to be considered part of government debt, when in 2016, the same NDC government restructured about GH¢2 billion debt owed commercial banks under 'the VRA Phase 1 Restructuring Program' using ESLA proceeds as a payment source. If 'VRA Phase 1' and TOR debt restructuring were deemed prudent at the time by the NDC and treated as a non-sovereign transaction, why not the E.S.L.A. PLC's Bonds? The inconsistency in the opinions of the Minority NDC is baffling."

Furthermore, in May 2023, the government, in its request for an IMF extended credit facility (ECF), promised the IMF that:

"Debt reporting will include details on contingent liabilities, ***including key SOEs with substantial fiscal risks*** such as COCOBOD, ECG, VRA, GWCL, TOR, GNPC, GNGC, and BOST; any collateralized debt issuance will be limited and closely monitored. … detailed data on all new external debt (concessional and non-concessional) contracted or guaranteed by the central government and the ***public entities*** mentioned in 8 (i.e., paragraph 8)[2] will be provided by the MOF (ministry of Finance) on a monthly basis, within 30 days from the end of each month."

In its May 2023 debt sustainability analysis for Ghana, the IMF stated that:

"The IMF's Debt Sustainability Analysis (DSA) for Ghana covers **public and publicly guaranteed** (PPG) debt of the central government. The DSA also includes (i) ***explicitly guaranteed*** debt of other public and private sector entities, including state-owned enterprises (SOEs) and (ii) certain ***implicitly guaranteed*** SOEs debt. … It also includes: (i) Cocobills which are issued domestically by Cocobod, and (ii) **the stock of domestic arrears to suppliers like independent power and gas producers (IPPs)**."

What does the IMF mean by implicitly guaranteed SOEs debt? Why should the debt of SOEs be included in public debt if they are not explicitly backed by sovereign guarantee (i.e., an obligation by the government of Ghana to pay the debt if the SOE defaults)?

To answer the questions above, imagine that an independent power producer like AKSA threatens to stop supplying power because the ECG has defaulted on payments for power supplied by AKSA. This would trigger the government's intervention. If AKSA were to threaten to sue the ECG or attach the ECG's assets (via a court order), the government would have an interest in the matter. The ECG is a "**too-important-to-fail**" state-owned enterprise. Therefore, in reality, there is an implicit guarantee by the government of Ghana which is, in effect, an explicit guarantee behind closed doors (e.g., see appendix). The absence of a *de jure* guarantee of the ECG's financial obligation by the government of Ghana does not imply the absence of a *de facto* guarantee by the government, an implicit guarantee that is driven by the economic reality of the ECG's "**too-important-to-fail**" status. Legal technicalities (e.g., special purpose vehicles like ESLA Plc; no sovereign guarantee clauses in contracts of SOEs, etc) are not efficient responses to economic realities.

The preceding discussion is related to how credit rating agencies determine the credit risk of a country. For example, Moody's assigns its lowest credit rating to a country if its interest payments as a percentage of revenue is more than 30%. Moody's assigns a weight of 25% to this

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[2]The public entities mentioned in paragraph 8 were (i) Tema Oil Refinery; (ii) Ghana National Petroleum Company; (iii) Ghana National Gas Company; (iv) Volta River Authority; and (v) Electricity Company of Ghana; (vi) Ghana Grid Company Ltd (GRIDCO); (vii) Ghana Water Company Limited; (viii) Ghana Infrastructure Investment Fund (GIIF); and (ix) Daakye. PLC, (x) Energy Sector Levy Act (ESLA). PLC, (xi) Asanti Gold Corporation; (xii) Cocobod, excluding the annual syndicated trade financing facility (xiii) Ghana Integrated Aluminium Development Corporation (GIADEC) and (xiv) Bulk Oil Storage and Transportation (BOST).

metric (i.e., interest payments as a percentage of revenue). Moody's explains the importance of this metric as follows:

"A high ratio of interest payments to revenue means that a large share of revenue needs to be diverted to interest payments, **crowding out other types of government spending, including on the provision of basic services, education, and health and safety**. The lower the sovereign's debt affordability (i.e., the **higher** is the ratio of interest payments to revenue), the higher the **social costs of servicing debt**. Unsustainably high social costs of servicing debt may over time **undermine a sovereign's ability, and eventually its willingness, to service debt**." (Parenthesis mine).[3]

An SOE like the ECG provides a basic service (the supply of electricity), which is as important as the provision of education, health, and safety. In fact, without reliable supply of electricity, the provision of education, safety, and health will be at risk. The ECG's indebtedness to independent power suppliers (IPPs) affects its ability to provide electricity and increases the risks of the social costs that, as Moody's argues, can affect the government's willingness to service its non-SOEs debt. For example, if interest payments on Ghana's external debt are so high that the government has to choose between helping the ECG to pay its debt to IPPs (and prevent dumsor) and servicing Ghana's external debt, the government will choose to pay the ECG's debt, regardless of whether the ECG debt is backed by a sovereign guarantee. This was what Moody's meant by "Unsustainably high social costs of servicing debt may over time undermine a sovereign's ability, and eventually its willingness, to service debt." The negative effect of the debt of an SOE (e.g., ECG) on the government's ability to service its other debts explains why the IMF includes the debt of SOEs in public debt.

If we lived in a world in which our SOEs were well managed and independent, they had no cashflow problems, were profitable, did not depend on government bailouts, and easily serviced their debts, they would pose no fiscal risks to the government's ability to manage non-SOEs public debt. There may no need to include the debt of SOEs in public debt. Unfortunately, this is not Ghana's reality. This was why the IMF, in its May 2023 debt sustainability analysis, observed, among others, that (a) "Cocobod operations pose **fiscal risks** related to its heavy involvement in **extra-budgetary spending**"; (b) "Ghana's Cocoa Board (Cocobod) — the state-owned entity … — has **accumulated annual losses for <u>many years</u>**."; (c) "**SOEs are imposing a direct fiscal cost to the central government and are a major source of fiscal risks**. This reflects both weak institutional arrangements and unsustainable sectoral policies." and (d) "Shortfalls in the energy sector have been significant due to below-cost-recovery tariffs, large distribution losses, and excess capacity amid take-or-pay contracts. This has cost the central government some 2 percent of GDP **in transfers** per year since 2019 and has also led to **accumulation of payables to IPPs and fuel suppliers**."

[3]Moody's Investors Service (2022). Rating Methodology: Sovereigns, November 22, 2022.

In terms of holistic debt management, the Ivorian approach is instructive. According to a **February 2019** titled "Debt management in a challenging environment: Lessons from Côte d'Ivoire" by Adama Kone, the Ivorian Minister of Economy and Finance (January 2016 to September 2019):

"Côte d'Ivoire's approach to debt management is consistent with the Guidelines for Public Debt Management published by the World Bank and the International Monetary Fund, which includes, importantly, ***the need for coordination among relevant branches of the government***. To this effect, the government set up a National Public Debt Committee (NPDC) — an inter-ministerial committee chaired by the Minister of Finance — as a coordinating entity to ensure consistency of public debt policy with fiscal and monetary policies. .... ***The government is also alert to the risks of debt accrued by public enterprises and other public sector entities. A centralized and comprehensive debt database has been set up to facilitate the monitoring of public enterprise debt and to ensure that these debts are taken into account in the national debt strategy***." (https://www.brookings.edu/blog/africa-in-focus/2019/02/13/debt-management-in-a-challenging-environment-lessons-from-cote-divoire/)

Ghana must take holistic debt management seriously.

Appendix

November 23, 2020: "The Chamber of Independent Power Producers, Distributors and Bulk Consumers (CIPDiB) have taken note of the reportage with the above headline carried on www.citinewsroom.com which, among other things, **quotes the Honorable Deputy Minister of Energy, Hon. William Owuraku Aidoo, as accusing the Chamber of IPPs as exhibiting traits of a pressure group and creating unnecessary tension with threats to interrupt power supply**. **We wish to assure government** and the public that we have no political motives for the timing of the communication that IPPs may be forced to shut down. This is based purely on commercial exigencies we currently face and not any political agenda"

Deputy Minister for Energy in charge of power, William Owuraku Aidoo: "The Chamber is being used as a pressure institution to pressure government into doing things that it is already doing; **having one on one discussions with individual power producers and so on**. With three weeks to elections, it is very unfortunate to hear this Chamber of Independent Power Producers coming out to say they will pull the plug on us, creating unnecessary panic within the system. **My recent interaction with them** shows there is no cause for alarm, so it is very worrying that they will come out and say things the individual power producers are not saying" (https://citinewsroom.com/2020/11/we-have-no-political-agenda-we-only-want-debt-cleared-ipps-to-government/)