

STATEMENT TO PARLIAMENT

ON THE IMPLICATIONS OF THE FALL IN CRUDE

OIL PRICES ON THE 2015 BUDGET

SUBMITTED BY

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12TH MARCH, 2015

IMPLICATIONS OF THE FALL IN CRUDE OIL PRICES

ON THE 2015 BUDGET

(THURSDAY, 12TH MARCH, 2014)

A. INTRODUCTION

1. Rt. Hon. Speaker and distinguished Hon. Members, I appear before you today to apprise Parliament and, through you, the people of Ghana on the implications of the decline in crude oil prices and its likely impact on the 2015 Budget. The purpose of the Statement is also to inform you of the steps Government has been taking to address the said issue to ensure that the macroeconomic objectives of Government is achieved.

2. Mr. Speaker, it is important to stress that the steps which Government is taking are in line with measures and policies approved by this august House in the 2015 Budget.

3. Following my appearance before this House in November 2014 and the subsequent approval of the 2015 Budget, the sharp decline in crude oil prices on the world market, has posed and continue to pose a challenge to the achievement of the 2015 economic programme. After careful consideration of these developments and the likely impact on revenues, Government has started to intensify the implementation of approved measures to ensure that MDAs and MMDAs remain within the lower than expected projected revenues.

4. Mr. Speaker, these fiscally prudent and responsible steps demonstrate the resolve of Government to implement policies to foster the attainment of the overall macroeconomic objectives outlined in the 2015 Budget. Furthermore, this will safeguard the achievement of the country's bright medium-term prospects for the benefit of all Ghanaians. Mr. Speaker, it is important to note that, the impact of the decline in crude oil prices and the adoption of measures to address it is not peculiar to Ghana.

5. The measures being taken by Government are also informed by the fact that recent volatilities in cocoa and gold prices affected the country's reserves and fiscal revenues negatively. In particular, they have contributed to the setbacks in the achievement of our macroeconomic objectives for the past two years. Likewise the impact of the shortfall in oil output in 2012, which contributed to the fiscal slippages that the Ministry of Finance has been addressing with some success since 2013.

6. It is, therefore, economically prudent to assess the impact of such commodity price volatilities on the economy on a timely basis—and as soon as they arise—and to take the required adjustment measures in order not to jeopardize the achievement of our macroeconomic objectives.

7. Mr. speaker, our approach and strategy has been to brief you, the people's representatives, and the general public through press briefings on developments in the economy in line with our laws and best practice.

B. IMPACT OF THE DECLINE IN PETROLEUM PRICES ON THE 2015 BUDGET

8. Mr. Speaker, crude oil prices have been falling since July 2014, with significant declines recorded from October 2014 when the Petroleum Benchmark Revenue for the 2015 Budget had already been estimated in accordance with the Petroleum Revenue Management Act (PRMA), 2011 (Act 815). In addition, the preparation of the 2015 Budget was far advanced. It is significant to emphasize that the PRMA requires the appointment of a consultant to certify the Benchmark Revenue by 1st September of each fiscal year to inform the preparation of the Budget.

9. Against this background, and given the slide in crude oil prices, the best we could do was to give a hint in the 2015 Budget, which we did, of a likely return to Parliament to address this phenomenon that had not been experienced in decades. We also indicated that we will be bringing amendments to the House for a review of the PRMA—including, where necessary, allowing some discretion for Minister of Finance to vary the Benchmark Revenue with the approval of Parliament. To address this legal bottleneck, we will be laying a bill on the amendments to the PRMA.

10. The decline in crude oil prices is mainly as a result of:

a. increased global production partly emanating from increased shale petroleum production, particularly in the United States, and OPEC's reluctance to cut crude oil production; and

b. low global economic activity which has led to low crude oil demand, with China (the world's leading energy consumer) and the other BRIC countries experiencing moderate growth.

11. Although crude oil prices have started showing signs of recovery in recent weeks from a low of US\$47 per barrel in January, many market analysts believe that near-term crude oil

prices could hover around an average of US\$50 per barrel in 2015. This is attributable to the bearish sentiments that have resulted from the persistence of the factors enumerated above. The International Monetary Fund (IMF) has recently revised its Brent crude oil price projection for 2015 to an average of US\$52.8 per barrel.

12. Mr. Speaker, in contrast, the Petroleum Benchmark Revenue (PBR) price in the 2015 Budget, based on the formula stipulated in the Petroleum Revenue Management Act (PRMA), 2011 (Act 815), was estimated at US\$99.38 per barrel and a volume of 102,033 barrels per day was also estimated in pursuant to the Act.

13. Based on these assumptions, the estimated total petroleum receipts for the 2015 Budget amounted to GH¢4.2 billion. Of this amount, GH¢2.5 billion was allocated as Annual Budget Funding Amount (ABFA) to finance specific projects and programmes in the Budget; GH¢1.1 billion was estimated to be transferred into the Ghana Petroleum Funds; and GH¢697.7million to the National Oil Company.

14. Following global developments and market sentiments which have led several international institutions to revise their oil price projections, it is not likely that the Benchmark price estimated for 2015 will be realized. As a result it has become necessary to critically examine the estimates of petroleum revenues in the 2015 Budget and assess the likely impact of such an examination on the Budget.

15. Consequently, the assessment by Government is based on a price of US\$52.8 per barrel, which is consistent with the IMF forecast. However, following discussions with the oil production companies, oil output is expected to remain unchanged at the 102,033 barrels per day used in the 2015 Budget. The practical implication is that the periodical ceilings given to MDAs and MMDAs are being revised downwards on account of the likely shortfall in petroleum revenues.

Impact on Total Revenue and Grants

16. Mr. Speaker, based on the new revenue assumptions, total petroleum receipts for 2015 is estimated at GH¢1.5 billion (1.1 percent of GDP), compared with the 2015 Budget estimate of GH¢4.2 billion (3.1 percent of GDP). The difference of GH¢2.7 billion is 64.4 percent lower than the 2015 Budget target. Of the projected total petroleum receipts, GH¢468.9 million will be transferred to the National Oil Company in line with the PRMA. Hence, the remaining amount of GH¢1.0 billion (0.8 percent of GDP), will not be sufficient to cover the Annual Budget Funding Amount of GH¢2.5 billion in the 2015 Budget.

17. Among the various sources of petroleum revenues in the PRMA, the significant decline in total petroleum receipt is mainly attributed to substantial decline in corporate income tax from oil companies. This is because the production costs for some of the companies will outstrip their revenues and result in losses.

18. Mr. Speaker, in addition to the direct impact on petroleum receipts, the decline in crude oil prices is also likely to impact negatively on the Special Petroleum Tax (SPT). Thus, the revenue yield from the special petroleum tax is estimated to be lower by GH¢185.6 million.

19. Mr. Speaker, the fall in crude oil prices—as well as the current energy situation and rapid depreciation of the cedi in 2014—could also have a negative impact on overall output. As a result, it is considered that taxes on domestic goods and services as well as non-oil taxes on income and property could be lower than what the 2015 Budget estimated by GH¢358.7 million.

20. Due to these factors, total domestic revenue for 2015 is now expected to be GH¢27.8 billion, resulting in a shortfall of GH¢3.1 billion.

21. Mr. Speaker, a factor that is expected to minimise the impact of the decline in crude oil prices is enhancement of grant disbursements following staff-level agreement reached with the IMF. Our development partners have pledged to disburse additional grants totalling GH¢381.1 million to fund programmes in the 2015 Budget. Therefore, on a more positive note, this could result in an increase in the estimate for grant disbursements from GH¢1.6 billion to GH¢1.9 billion.

22. In summary, total revenue and grants for the 2015 fiscal year are now expected to be GH¢29.7 billion (22.3 percent of GDP) instead of GH¢32.4 billion (24.0 percent of GDP), resulting in a shortfall of GH¢2.7 billion (1.7 percent of GDP).

C. PRECAUTIONARY STEPS IN IMPLEMENTATION OF THE 2015 BUDGET

23. Mr. Speaker, the Government has been intensifying the implementation of measures approved in the 2015 Budget. The purpose is to address the revenue shortfalls noted above, ensure the achievement of the objectives of the ongoing fiscal consolidation, and keep borrowing in line with the levels approved in the 2015 Budget.

24. The key measures include an across the board reduction in expenditure ceilings on Goods and Services and Capital by GH¢344.0 million and GH¢868.4 million, respectively, as well as a drawdown from the Ghana Stabilization Fund. However, these measures are designed to protect social spending.

25. Similarly, transfers to the Ghana National Petroleum Company (GNPC) from Government's carried and participating interest in oil will be reduced to GH¢468.9 million.

26. In summary, the estimate for total expenditure and arrears clearance for 2015 are expected to decline by GH¢1.5 billion from GH¢41.2 billion (30.5 percent of GDP) to GH¢39.7 billion (29.8 percent of GDP).

27. Based on these expected changes in total revenue and grants as well as total expenditure and arrears, the fiscal deficit for 2015 is estimated to be GH¢10.0 billion (7.5 percent of GDP), up from the 2015 Budget target of GH¢8.8 billion (6.5 percent of GDP).

28. In line with the formula specified in section 12 of the PRMA, it is expected that an amount of GH¢487.2 million would be drawn from the Ghana Stabilization Fund, on a quarterly basis to finance the gap. Mr. Speaker, the drawdown of the GSF is significant in one major respect: it bears testimony to our efforts at building fiscal buffers in our public financial management. It is in times like these that we are able to reap the benefits of making a conscious effort at building the GSF. This underscores the need to build the GSF as was announced in the 2015 Budget.

29. Mr. Speaker, it is important to note that the GSF had accumulated in excess of US\$590 million both in capital and interest incomes between 2011 and 2014. In similar vein, we expect to see the benefits of other initiatives such as the establishment of the Ghana Infrastructure Investment Fund (GIIF) and the Ghana EXIM Bank.

30. Mr. Speaker, besides the drawdown from the Stabilization Fund, the fiscal deficit will be financed from domestic and foreign sources.

31. Domestic financing of the Budget is estimated at GH¢6.4 billion, lower than the 2015 Budget estimate. It is expected that this will free up more resources for the private sector and reduce government's domestic interest costs burden.

32. Foreign financing of the deficit is estimated at GH¢3.0 billion. Of this amount GH¢1.7 billion will be sourced through the issue of a Eurobond (in addition to an estimated US\$500 million that is expected to be used to refinance the 2007 Eurobond). We will come to this august House to seek approval for the issuance of the said Eurobond, in line with the two-year market policy approved by the House in the 2014 Budget.

Other steps being implemented by Government

33. Mr. Speaker, we will continue to strengthen the Public Financial Management system and deepen structural reforms in the public sector as part of the overall objective of ensuring transparent and accountable economic governance.

34. To make the reduction in expenditures effective and ensure the achievement of our fiscal objectives, the Ministry of Finance has issued Budget Implementation Instructions to all MDAs to ensure that the following measures are implemented:

i. Transfers to Statutory Funds will continue to be aligned to central government programmes. Furthermore, Statutory Funds are to continue limiting the award of new contracts and focus on the clearance of existing commitments in accordance with Government policy;

ii. The expenditure ceilings are being enforced through implementation of quarterly budget allotments on MDAs budgets. In this regard, expenditures will be prioritized by the MDAs based on the budget allotments. Requirements for Specific Warrants and Commencement/Continuation Certificates under the GIFMIS will ensure that capital expenditures are within the new limits;

iii. Continuation of the policy on limit on the award of new contracts by MDAs as well as the curtailment of extensions and variations in ongoing projects will be enforced; and

iv. Government has started disallowing the award of MDA and MMDA contracts with provisions that allow for indexation in foreign currency. Also some of these institutions denominate local costs in foreign currency. In exceptional circumstances where contracts need to be awarded in foreign currency, prior approval must be obtained from the Ministry of Finance. In this regard, companies which have existing contracts denominated in foreign currency and who incur foreign exchange losses are reminded to claim such losses as allowable expenses under the income tax laws. This is also in line with accounts prepared under International Financial Reporting Standards (IFRS) and International Public Sector Accounting Standards (IPSAS). Consequently, no claims for forex losses will be entertained.

35. Mr. Speaker, as noted in the 2015 Budget, the weaning off of some subvented agencies from Government payroll has begun. Three agencies, namely; the Energy Commission, the Environmental Protection Agency (EPA), and the Driver and Vehicle Licensing Authority (DVLA), which have the capacity to be financially independent based on their Internally Generated Funds (IGFs) have been identified for weaning off this year. Nine other agencies are being reviewed for implementation in subsequent years.

36. Mr. Speaker, the Controller and Accountant General's Department in collaboration with the Ministry of Finance and other agencies continue to implement reforms to address the payroll and HR challenges in the public service. These reforms are being implemented to check the size of the compensation bill which is being gradually brought within budget constraints, thereby providing funding for other important national priorities. Government commits to tighten control of the payroll.

37. Following the Ho Forum on the sustainability of the Single Spine Pay Policy, a number of pay roll and Human Resource (HR) measures have been put in place to address existing weaknesses. In addition, Cabinet has constituted an Inter-Ministerial Committee on payroll clean-up to identify areas for improvement in the payroll and Human Resource administration and to recommend measures to address them. Payroll reforms which are currently being implemented include:

a. The provision of monthly Payroll reports to all Sector Ministers for verification and validation. The exercise is aimed at informing Sector Ministers and heads of MDAs of the status of their payroll to ensure that they check the payroll and HR management issues in their various units;

v. from the Ministry of Finance. In this regard, companies which have existing contracts denominated in foreign currency and who incur foreign exchange losses are

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- b. The provision of monthly Payroll reports to all Sector Ministers for verification and validation. The exercise is aimed at informing Sector Ministers and heads of MDAs of the status of their payroll to ensure that they check the payroll and HR management issues in their various units;
- c. The CAGD has also initiated an exercise to update the bank account details of employees on the mechanized payroll system as part of reforms to clean the mechanized payroll data. The names of employees with zero bank accounts numbers were identified and suspended from the payroll system. As at the end of February 2015, 44,496 names out of the total number of 47,186 employees were validated by the Audit Service and restored onto the payroll. The records of the remaining 2,690 employees who did not submit the required documents were suspended from the payroll permanently and are to be investigated for appropriate sanctions to be applied;
- d. The CAGD has also begun another exercise to suspend the salaries of employees on the mechanized payroll without Social Security numbers. Opportunity has been provided to employees on the mechanized payroll to update their record by end of March after which the names will be permanently expunged;
- e. Following the success in using the E-Switch for public sector wage payments, the exercise has been extended to the payment of allowances of National Service Personnel and will be extended to all employees on the mechanized payroll. The aim of this exercise is to validate

employees using the E Switch database. For the month of February 2015 the National Service Secretariat paid its personnel on E-switch cards. The exercise will ensure a single identity for each employee on the payroll;

- f. In line with government policy to use ICT to drive business processes in the public service, the CAGD has developed and deployed an Electronic Salary Payment Voucher System (E-SPV) for use by heads of MDAs and MMDAs. Validation and certification through the E-SPV system has now become a pre-condition for payment of salaries to employees. The automation has addressed the delays in updating the payroll and in particular the deletion of separated staff from the payroll. Unit heads, thus, determine who should be paid for a particular month. The E-SPV System has been deployed in 4 regions, namely Greater Accra, Ashanti, Brong Ahafo and Northern regions. Nationwide rollout of the E-SPV system is expected to be completed by June, 2015;
- g. These measures are designed to decentralize the payroll management to the district and unit level. The aim is to empower Heads of MDAs and MMDAs to have full access to their payroll data to enable them exercise control over their payroll cost; and
- h. Integration of the payroll system into GIFMIS Financials and GIFMIS Hyperion has been completed. This is to facilitate monitoring and strengthen budgetary control over payroll. Furthermore, the integration with the HRMIS is ongoing and expected to be completed in June 2015.

41. Mr. Speaker, the emphasis on payroll and HR is important because it constitutes the largest single item in the Budget and as is well known has been plagued with many problems in the past.

D. UPDATE ON PROGRAMME WITH THE INTERNATIONAL MONETARY FUND

42. Mr. Speaker, permit me to provide a brief update on the status of the negotiations with the IMF for a Fund programme. We have been in negotiations with the IMF and subsequently held four rounds of negotiations with the IMF. During the last visit of the Fund mission to Ghana from 19th to 26th February 2015, Government reached staff-level agreement with the Fund subject to approval by IMF Management and the Executive Board.

43. The programme will be supported by a three-year Extended Credit Facility (ECF) arrangement. The proposed access to Fund resources which is for Balance of Payment support could total SDR 664 million (about US\$940 million), or 180 percent of Ghana's IMF quota.

44. Rt. Hon. Speaker, I am happy to inform you that the IMF Executive Board is scheduled to meet in early April to consider and approve Ghana's programme with the Fund.

E. CONCLUSION

45. Rt. Hon. Speaker, as noted in the 2015 Budget, the medium term prospects of the economy remain bright. This is supported by expected additional oil and gas production, enhanced services sector performance, and improvements in agriculture, among others.

46. Mr. Speaker, I wish to conclude by emphasizing that government will continue to work tirelessly to ensure that these positive prospects as well as our macroeconomic stability and socio-economic objectives are not derailed by external and domestic shocks. Our resolve to address the impact of these shocks has once again been demonstrated by our quick reaction in putting in place remedial measures to address, where necessary and as presented to you today. Mr. Speaker, may I repeat that it is the fiscally prudent and responsible thing to do—and in line with the regular reporting or briefing that this House deserves.

47. Mr. Speaker, it is our conviction that the measures we have put in place to address the impact of these shocks will yield the intended benefits and significantly contribute to the achievement of our short-to-medium term fiscal consolidation objectives.

48. Mr. Speaker, in the course of this year, I will on behalf of H.E the President come back to this august House for a mid-term review of the 2015 Budget.

49. Rt. Hon. Speaker, I wish to thank you and members of the House for granting me the privilege to address the House.

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