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An Assessment of the Proposed US$50 Billion Century Bond for Ghana

1.0 Introduction

The Minister of Finance has disclosed that the 2019 Budget will announce the issuing of a US$50 billion century bond that will provide resources to help address major challenges confronting the country, including the cedi depreciation, infrastructural deficit, and low industrial development. A successful century bond will make everybody comfortable about the future of the country's needs for both infrastructure and foreign exchange, so that we have a lot more stability. According to the Minister, the bond will be raised in bits through a shelf offering, which will allow issuers to register a security without selling the entire issue at once.

The Minister's disclosure followed an announcement made by the President last month in China. With the country exiting the IMF program by the end of the year, the President stressed that Ghana is determined never to return to the Fund-support program. In order to do so, the government is looking seriously at how it can secure sources of long-term finance that will allow it to deal with the country's infrastructure development and also realize the vision of a "Ghana beyond Aid". To this end, the Ministry of Finance is considering floating an ultra-long-term-bond.

This paper reviews the government's plan to issue a US$50 billion century bond to finance infrastructure and other development projects and offer some suggestions for that initiative.

2.0 Why Sovereign Century Bonds?

National governments have been issuing bonds for centuries. Today, sovereign debt forms an important cornerstone of many institutional investment portfolios, and is becoming increasingly popular with many individual investors. In April 2016, France issued a 50-year bond for the first time, dramatically increasing the length of its outstanding debt. Remarkably, it managed to find buyers for the debt, on a yield of 1.9%, with repayment scheduled for May 2066. But this is not the longest duration for a bond issued. In October 2010, Mexico issued a US$1.0 billion 100-year bond denominated in US dollars, with a yield of 6.1%. In August 2015, Belgium issued its first ever century bond. Ireland followed suit in March 2016, raising €100m at a yield of 2.35%. In June 2017, Argentina joined with a US$2.75 billion century bond with a yield of 7.9%. The Spanish and the Italians have both gone above 45 years, and will probably join the century club as soon as they think they can get away with it (Smith, 2018).

Long-term bonds give a predictable source of income for buyers and funding cost for the issuers. For a given amount of borrowed funds, the annual payment is lowest when the repayment period is stretched out. Bond investors, however, would likely demand higher yields on longer-maturity bonds to compensate for government debt and inflation risks. But as yields rise, it becomes harder for the issuer to reap any costs-saving from the program. Long-dated bonds also ease roll-over risks. If a country issues mostly short-term debts, the roll-over problems happen almost constantly. However, if there are more long-term debts, including 100-year bonds, it provides some relief from roll-over problems. Also, during their life, the value of a long-dated bond will move inversely with the interest rates. So, if interest rates are perceived to be stable or at the low end of their maturity period, it makes sense for a government to issue a long-dated bond. On the other hand, if interest rates turn out to be higher than the average, long-dated bonds are a better deal for the buyer than the issuer. Thus, long-dated bonds fund development at low rates, thereby saving money.

The decision to issue long-dated bonds is influenced by considerations of image and prestige rather than technicalities. A successful 100-year issue is deemed an indication of investor confidence in an economy. For an emerging market eager to establish a firm investor base, this is a considerable attraction. Although the trend is moving toward these longer-dated issues, they trade more like shorter-dated bonds and there is little difference in risk or technicalities (Garner, 1997; Langager, 2018). For a bond which has a reasonable coupon the longer payment almost becomes irrelevant. There are also some institutional investors which use century bonds to lengthen the duration of their bond portfolios to fulfill certain duration-based goals. These include pension funds and life insurance companies, institutions that need assets to match their liabilities stretching into the future for many decades.

When a sovereign government needs to borrow to fund its operations, it may choose to denominate bonds in a more stable and marketable currency. Borrowing in a foreign currency however exposes a country to exchange rate risk. If the local currency drops in value, paying down international debt becomes considerably more expensive. If a government is not able to mobilize more domestic revenue or lower its level of spending over time, there is always a risk that it could default on its debt repayment. In such a situation, the government may decide to roll over its debt by issuing new bonds to replace those that reach maturity. But if investors begin to lose confidence in the management of the country's finances, they are likely to look for other investment opportunities or demand higher yields. For these reasons, government bonds, and particularly those issued in a foreign currency, tend to draw a high level of scrutiny from investors.

3.0 Ghana's Proposed US$50 Billion Century Bond: Comments

The proposed US$50 billion century bond for Ghana raises a number of concerns. Key among these concerns is the size and the length of the bond. No African country has issued a century bond yet, and only a handful have sold 30-year debt in the last couple of years. In South America, only Argentina, Brazil and Mexico have issued 100-year dollar bonds since 2010, of which Argentina's US$2.75 billion was the largest. But, Argentina, which like Ghana is rated B by Fitch Ratings Ltd., sold its US$2.75 billion century deal in June last year in much better market conditions. Argentina also has a much bigger economy. Its GDP of US$637 billion in 2017 was almost 11 times bigger than the GDP of Ghana, which was recently rebased to US$58.9 billion. Total public debt equaled 65.9% of the old GDP at end of July this year, compared with 67.4% at the same time last year.

External debt totalled US$18.2 billion, about 54% of the total public debt. Although, the rebased GDP figure of GH¢256 billion for 2017 brings the country's debt/GDP ratio to 62.3%, this does not indicate a significant improvment in the country's debt dynamics. It is therefore uncertain whether investors will have the appetite to buy a US$50 billion 100-year Ghanaian bond.

Last year, Ghana spent GH¢13.57 billion in interest payments and GH¢4.9 billion in amortization, implying that debt-service costs alone amounted to GH¢18.47 billion, representing 46.2% of total domestic revenue for the year. The country's ability to refinance these interest payments and reduce the cost of borrowing by even 10% will translate into about GH¢1.1 billion in savings annually. Also, that 30% of the country's total debt stock is in treasury bills and other short-term instruments of less than one year means that there is a constant need to roll the debt over on maturity. This is a problem that can be eliminated by extending maturities and reducing the country's short-term borrowing. But a US$50 billion century bond with interest of say 5% per annum is not the solution, as this will translate to a debt-servicing cost of US$2.5 billion per annum, or US$250 billion in 100 years.

Another issue is whether the government can generate enough domestic revenue to support the debt-servicing and repayment costs of the US$50 billion century bond being contemplated. It is indeed a serious failure on the part of the country that any time it needs money to finance capital projects, it has to resort to borrowing rather than relying on domestic revenue.

A recent statement issued by the IMF says that Ghana's growth prospects remain strong, supported by robust oil and cocoa production, while inflation has remained in single-digit. This led the rating agents to upgrade the country's ratings from B- to B with a stable outlook. Ghana has, however, been affected by the volatile environment for emerging and frontiers markets, which has exerted pressure on the cedi, resulting in a steep depreciation. The cedi depreciated by 7.3% in the first nine months of this year compared to 4.4% in the same period last year (see IMF, 2018).

Ghana is also still at a high risk of debt distress, despite the recent policy measures introduced to tame the fiscal deficit. Total public debt equaled 65.9% of the old GDP at end of July this year, compared with 67.4% at the same time last year. External debt totalled US$18.2 billion, about 54% of the total public debt.

As the Institute for Fiscal Studies (IFS) has persistently pointed out, domestic revenue has always fallen short of budget targets in the country, with the revenue gap increasing significantly in the last few years. The recent rebasing of GDP which saw the country's output rising from GH¢123.6 billion in 2013 to GH¢256.7 billion in 2017, reduced the domestic revenue/GDP ratio to between 15.1% and 16.7%, with an annual average of 15.6% during the period. This indicates that, Ghana continues to remain far below the levels of its regional peers, suggesting that the country's actual revenue is far short of what its economic potential should generate.

Ghana's fiscal indicators during the first half of this year point to a continuous revenue underperformance.

Yet, the "Ghana beyond Aid" agenda of the government implies "self-reliance", the use of the country's own resources to support its development. This calls for a robust and effective strategy for domestic revenue mobilization, and not a reliance on foreign sources for development finance.

Ghana's development cannot be tied exclusively to the issuing of foreign loans, which have serious implications for macroeconomic performance, domestic savings, and foreign exchange. Government will therefore need to address the persistent revenue shortfalls in a very serious manner, instead of finding consolation in issuing bonds.

As recently observed by the IMF (2018), access to new financing arrangements and longer-term debt instruments would help fund Ghana's pressing development and infrastructure needs. Such arrangements, however, would need to be based on a well-designed national development plan that would be implemented in a transparent manner to deliver value for money and be consistent with the country's debt sustainability considerations. Fortunately, the National Development Planning Commission (NDPC) has prepared a 40-Year National Development Plan (2018-2057) and a 30-Year Infrastructure Plan (2018-2047) for the country. The government has also launched a Public Investment Management System (PIMS) to ensure effective and efficient management and delivery of infrastructure projects. The PIMS is designed to enhance the quality of public investment by strengthening the links between the national medium-term development policy framework, national infrastructure and sector plans, and the annual budget. The Ministry has also established a high level Public Investment Planning (PIP) Working Committee that is charged with the responsibility to review all government projects, prioritize and rank them to feed into a pipeline of projects for Cabinet consideration.

The IFS is of the view that, the work of the PIP Committee should not be limited to a review of the currently scattered projects across the country to inform government policy and strategy. The Committee should also work closely with the NDPC to review all plans that have been developed, with a view to incorporating them into one long-term national development plan and subject it to public discussion for adoption and implementation. Such widespread public consultations will create opportunity for Ghanaians to examine the relevance and comprehensiveness of the plan, the strategies for its execution, as well as the programs and projects contained in it so that its implementation can be supported by all Ghanaians.

The fear that long-term funding will leave huge debts for posterity also underlines the need for a long- term national development plan. Once a long-term national development plan that seeks to grow the economy and develop the country is adopted for implementation, then issuing century bonds to finance the selected programs and projects will make every Ghanaian comfortable.

4.0 Suggestions

First, while it is necessary to explore various sources of funding to address Ghana's huge infrastructure gap and developmental challenges, a 100-year bond is ill-advised.

It would, in fact, be suicidal for the country to go for such a colossal bond that lasts 100 years without a blueprint that carefully outlines the development priorities of the country and how the funds would be used to add value to the vast resources of the country. Without such a blueprint, public confidence and support for a century bond will be low as this would create a huge debt overhang which could be disastrous for the country. The decision to issue a bond of this size and for such a long period must therefore be driven by a long-term national development plan that has received the blessing of all Ghanaians.

Second, the bond in question will be the world's biggest sovereign 100-year dollar-denominated debt to be issued at a time when emerging market dollar-bond sales are dwindling as rising U.S interest rates are dampening appetite for high-yielding assets. The average yields on emerging market dollar debt have also climbed almost 100 basis points since April 2018 amid a sell-off sparked by the recent crisis in Argentina and Turkey. The issue of the century bond should therefore wait until the country's fiscal consolidation and macroeconomic stability have gained strong ground and the cedi has strengthened. Even then, a US$50 billion century bond would be too much for a country with a GDP of under US$60 billion and would be a dangerous experiment that could harm future generations.

Third, as the IFS has pointed out several times, financing national development projects brings into view the need for strong domestic revenue mobilization. To achieve this, strategies and measures that seek to reduce the widespread tax exemptions and leakages, broaden the tax base, strengthen the revenue administration, improve tax compliance, help to combat abuses and corrupt practices are urgently needed. This will also require a serious review of the current oil and mining fiscal regimes and excessive tax incentives and concessions granted to operators in the free zones and state-owned enterprises.

The national identification and digital address system projects currently being implemented by the government are very critical as they will help to bring informal sector businesses under the tax net to help increase revenue mobilization.

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