Briefing
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Natural Resource Governance Institute

Funding Ghana's 'Free' Senior High School with Oil Revenue: Sober Reflection Required

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Article 25 of Ghana's 1992 constitution provides for equal rights to educational opportunities. The article also introduces progressively free education at the secondary level. Since 1951, Ghana has tried different policies and approaches to ensure free, compulsory, universal basic education, with varying degrees of success.

The New Patriotic Party's (NPP) 2016 election manifesto promised to redefine basic education to include senior high school (SHS), covering vocational, agricultural and technical schools, and make it available for free for all Ghanaians. Basic education in Ghana currently includes preschool, primary and junior high school. Through the 2017 budget statement, the government has indicated its intention to use petroleum revenues to extend free basic education to the secondary level—meaning SHS. This is touted as NPP's "Free SHS" policy. The government's 2017 annual budget and economic policy statement proposed funding the policy from the Annual Budget Funding Amount (ABFA) derived from petroleum revenues starting in September. In this briefing, we aim to shed light on various options that could be considered by the government in funding "Free SHS" with petroleum revenues, with a particular emphasis on how funding for the program can be rendered sustainable going forward.

Ghana is in dire economic straits. It faces a series of hurdles: low commodity prices; high costs of living; financial malfeasance (abuse of public funds cited annually in the auditor general's report); limited fiscal space; a lower sovereign credit rating; and ever-ballooning public debt; which is equal to about 74 percent of GDP. As a result, the country was forced to sign on to an International Monetary Fund bailout program projected to end in December 2017. Significant budget leakages accumulated through public spending inefficiencies pose further challenges to the economy.

The NPP made several campaign promises listing various development projects such as building factories and dams, an 814-kilometer railway from Accra to Paga, and the Zongo Development Fund (aimed at enhancing infrastructure development in impoverished inner city communities mainly inhabited by migrants from other parts of the country), among others. In the midst of Ghana's poor economic performance, these promises may necessitate developing other sources of funding, as well as sustainable financing for "Free SHS." The decision to use the ABFA has sparked countrywide debates over what, when and how Ghana invests petroleum revenues.

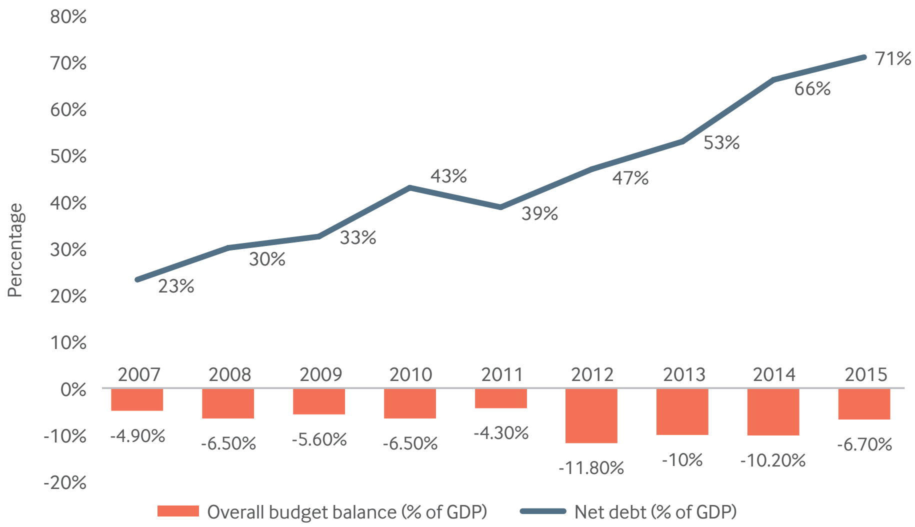

Figure 1. Net debt to GDP ratio versus budget deficit to GDP (2007-2015)

Figure 1 points to evidence of Ghana's growing economic challenges, with a high, rising debt-to-GDP ratio, potentially leading to higher interest payments.

Ghana's petroleum revenues present important opportunities to finance development. As this revenue stream is finite, there is a need for effective management, higher-return investment and equitable distribution of these returns. Civil society actors have raised concerns about the need for a national development plan or a coordinated strategy to guide petroleum revenue spending. This remains critical: the selection of areas and sectors to benefit from this revenue remains at the discretion of the finance minister. An investment by the new government in developing a consensus based plan would perhaps facilitate a more inclusive approach in selecting these priority spending areas. The "Free SHS" policy has heightened the importance of these debates.

Since oil production began in 2010, total petroleum receipts are approximately USD 3.2 billion—about 4 percent of GDP. Although this provides an additional stream of income for the government, it is relatively insignificant compared with non-oil revenues, most of which come from the mining and agriculture sectors. The national budget, through the ABFA, received the greatest share of petroleum receipts, followed by the Ghana National Petroleum Corporation (GNPC), the Ghana Stabilization Fund (GSF) and the GHF. (See figure 2.)

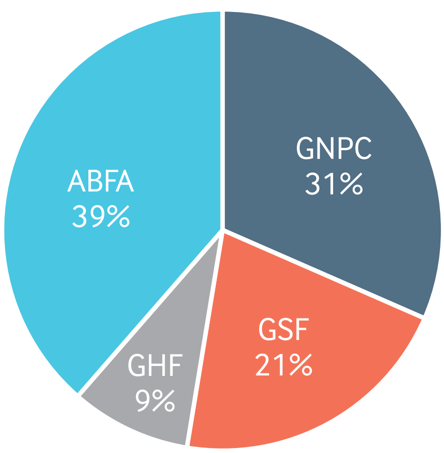

Figure 2. Allocation of Ghana's petroleum revenues (2011-2015)

The proposed "Free SHS" policy has raised important questions:

- How might access to and quality of education be increased?
- Can the economy accommodate the full cost of a free basic education that includes public preschool, primary school, junior high school and senior high school?
- How will the policy impact Ghana's current education infrastructure (e.g., school buildings, technology) deficit?
- How will the policy affect the quality of teaching and learning, as well as the distribution of teachers?
- How will the policy impact the short-, medium- and long-term costs of "basic education"?

The answers to these questions will inform a national consensus for an effective implementation strategy. The discussions will also allow for public buy-in on financing alternatives. While the government has not officially published an implementation framework, information in the public domain suggests that the policy is likely to cost about GHS 3.6 billion annually. Keeping Ghana's current economic realities in mind, the following options could be considered in funding "Free SHS" from petroleum revenues.

OPTION 1. ANNUAL BUDGET FUNDING AMOUNT (ABFA)

The ABFA is the amount of petroleum revenues allocated to support Ghana's annual budget. Over the last five years, the ABFA has totaled roughly GHS 3.4 billion, representing 39 percent of total petroleum receipts up to 2015. This means that, on average, ABFA receives about GHS 600 million annually. ABFA allocations have amounted to an average of about 4 percent of total government revenue and less than 3 percent of GDP since the inception of oil production in Ghana. Of these, roads and other infrastructure have constituted the chunk of 2011-2015 allocations (see figure 3). The ABFA is the medium through which the government is able to select and fund projects that will help in realizing Ghana's development objectives. However in the recent past, the government has been accused of "spreading too thin," as the ABFA has been used to either fully fund or co-fund several projects across priority areas selected by the finance minister.

In the 2017 budget, the government has proposed GHS 211 million from the ABFA be spent to finance "Free SHS" beginning in September 2017. This represents 27.3 percent of the ABFA for the year. ABFA funds would be supplemented by additional budgetary support of GHS 188 million to finance the balance of costs associated with the "Free SHS" commitment.

Moving forward, it would remain an option for the government to consider to funnel most or all future ABFA receipts into "Free SHS." This move would help improve implementation and oversight through stringent measures adopted in budget process. Using all ABFA receipts to finance "Free SHS" would, however, mean finding alternative financing for existing priorities. Depending on the breakdown of how much of the "Free SHS" spending is allocated to capital versus recurrent expenditures, any future plans to make "Free SHS" the overwhelming focus of ABFA spending may necessitate a discussion of potential amendments to the Act. Section 21(4) of the PRMA requires that no less than 70 percent of ABFA in a given year be spent on "public investment expenditures." Any plan that resulted in more than 30 percent of ABFA being dedicated to recurrent educational expenditure would therefore require a clear analysis of whether such spending qualifies as "public investment expenditure" under the law.

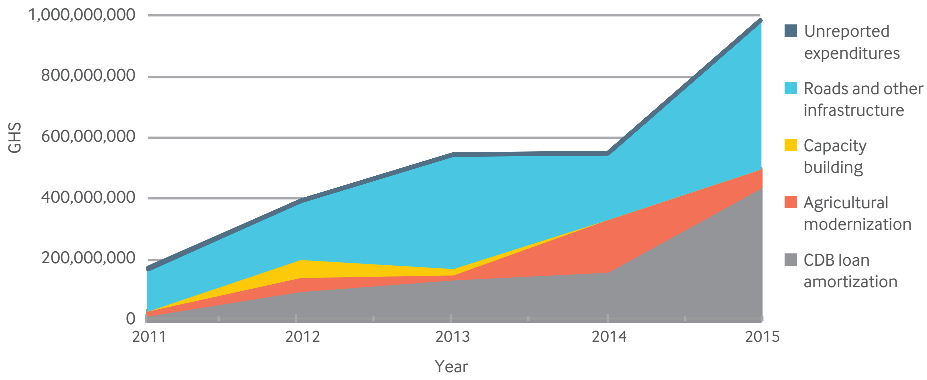

Figure 3. ABFA allocation 2011-2015

OPTION 2. CONSOLIDATION OF THE ABFA AND A PORTION OF THE ALLOCATION TO THE GHANA NATIONAL PETROLEUM CORPORATION (GNPC)

In future years, if the government wishes to carve out additional fiscal space to fund the sustainable implementation of the "Free SHS" commitment, it may wish to consider using a combination of ABFA and a portion of the kinds of revenues that have heretofore been allocated to GNPC. GNPC currently receives an allocation of up to 30 percent (between 2014-2016, Section 7(3) of the PRMA) of net cash flow from participating and carried interests after equity financing costs have been deducted. In the GNPC revenue retention model, the corporation enjoys flexibility in planning its spending over a three-year period; parliament reserves the right to reassess the corporation's allocation every three years. However, public perception is that GNPC possesses significant cash holdings that may not be truly representative of its spending capacity, due to substantial amounts invested by the GNPC in quasi-fiscal activities (non-oil related activities). Some portions of the revenues allocated to GNPC could be channelled through the budget process to support the implementation of "Free SHS." In addition to the aforementioned challenges associated with accessing ABFA, ceding money to the "Free SHS" program could compromise the GNPC's strategic objective to become a world-class operator capable of managing its own complex oil and gas projects. Reducing the revenues allocated to GNPC would also require Ghana to take additional steps to stimulate exploration in the sector in order to grow the country's resource base and stave off a decline in production currently anticipated by 2020-2021 (see figure 4).

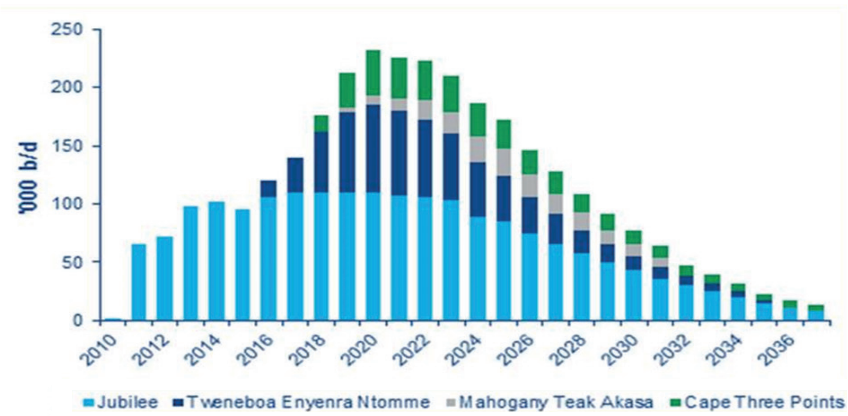

Figure 4. Lifecycle projections of Ghana's petroleum

Source: Wood Mackenzie

OPTION 3: GHANA HERITAGE FUND (GHF)

The GHF was established under the Petroleum Revenue Management Act (PRMA) to support future generations as petroleum reserves are depleted. It has received approximately 9 percent of Ghana's total petroleum revenue receipts. To date, the GHF has accrued USD 277 million (about GHS 1.2 billion) over five years—significantly less than the projected cost of one year of "Free SHS." As the government considers options for funding the "Free SHS" program beyond its initial year, it should take into account the reality that GHF alone would fall far short of being able to fill anticipated shortfalls. Petroleum revenues are volatile and tying the policy's funding to an oil-dependent source would negatively impact implementation (see figure 5). Uncertainties surrounding the revenues could worsen in years where there are oil price shocks. Given Ghana's growing recurrent expenditures, counting on the inadequate GHF funds to back the policy in the future could force the government to either borrow or cut other critical expenditures.

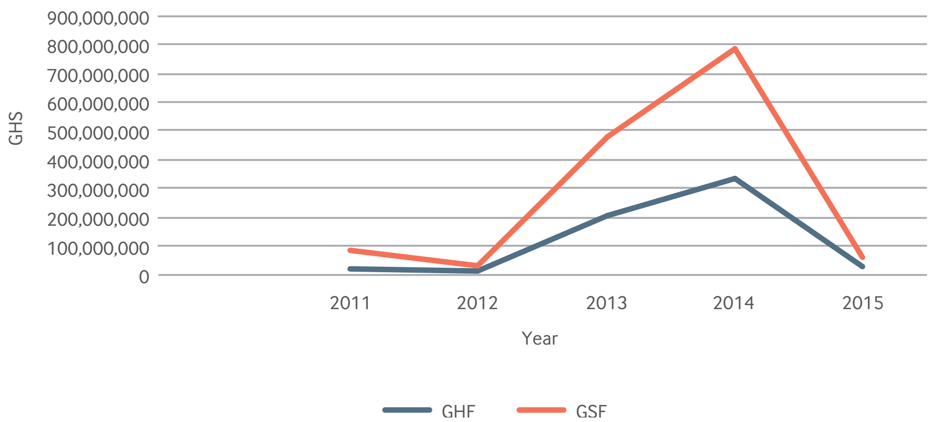

Figure 5: Petroleum Funds Allocations (2011-2015)

Beyond potential economic challenges, the government could face legal challenges in accessing the GHF. The PRMA bars any withdrawals from the GHF in the short-to-medium term. It only permits a partial withdrawal from interest accrued on the fund 15 years after the implementation of the PRMA—and then only with parliamentary approval. In practice, this means the government can only withdraw accrued interest from the fund from 2026 onward. Any attempt to withdraw from the GHF would require amendments to the PRMA.

Caution must be exercised in pursuing this option. International experience has shown that continuously altering the legislative framework for managing petroleum revenues leads to poor outcomes. This reinforces need for national dialogue on this decision, in keeping with broad consultations that brought about the GHF.

"Free SHS" is laudable: it seeks to improve Ghana's human capital base to advance national development. In pursuing its successful implementation through the use of petroleum revenue, broader national consultation and consensus is needed to carve out clear objectives, develop a coordinated implementation strategy detailing costs, and spell out achievable, measurable outcomes.