GHANA | MACROECONOMIC UPDATE | MONETARY POLICY | INSIGHTS

## FUNDAMENTALS

# GHANA MPC UPDATE: STAYING THE COURSE

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# IN BRIEF

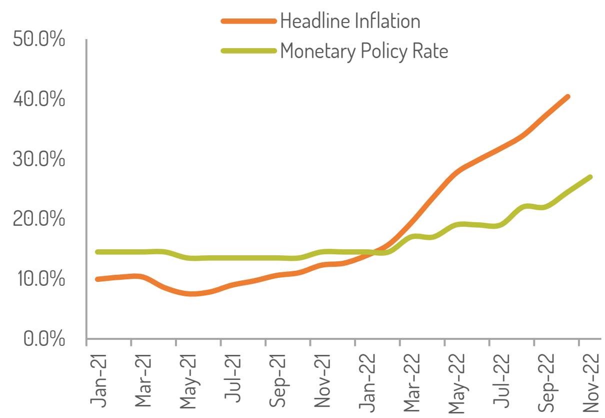
- The Bank of Ghana delivered a 250bps hike in the monetary policy rate to 27.0% at the November 2022 monetary policy committee meeting
- In view of the potential price pressures from the proposed tax measures in 2023 and a lingering FX uncertainty, we reckon a final policy rate hike of up to 200bps could be on the cards in 1Q2023
- A bearish near-term outlook on the external accounts, but debt restructuring could ease the pressure in 2023
- The weakening economic activity will culminate in a lower real GDP growth in FY2023
- Banking sector remains profitable but risk to financial soundness is mounting

## Bank of Ghana delivers a 250bps hike

At its November 2022 meeting, the Monetary Policy Committee (MPC) of the Bank of Ghana (BOG) delivered another strong response to the relentless increases in Ghana's consumer price inflation. The MPC hiked the policy rate by 250bps to 27.0%, the highest level since 2003 (IC Insights expectation: +200bps | Consensus: +175bps). The latest increase brings the cumulative hike in the monetary policy rate to 1,350bps since November 2021.

In line with our outlook, the MPC expects headline inflation to peak in 1Q2023 before declining to around 25% by the end of 2023 (IC Insights: 19.3% | GOG: 18.9% | IMF: 20.9%). However, the MPC cited upside risks to the outlook, mainly from the proposed VAT increase and exchange rate pass-through to inflation. In view of the potential price pressures from the proposed tax measures and lingering FX uncertainty, we reckon a final policy rate hike of up to 200bps could be on the cards in 1Q2023.

**INFLATION AND POLICY RATE PATH SINCE 2021**



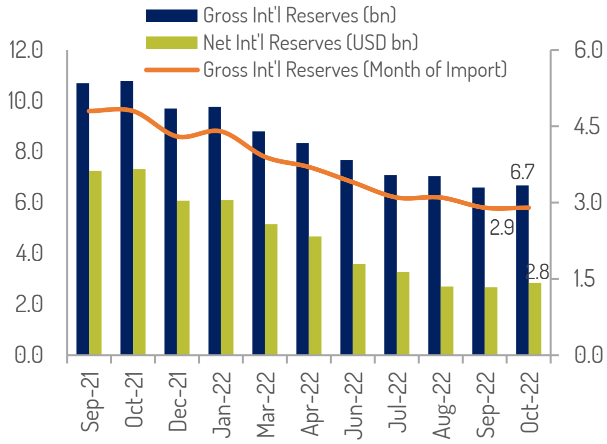

SOURCE: BANK OF GHANA, GHANA STATISTICAL SERVICE

**A bearish near-term outlook on the external accounts, but debt restructuring could ease the pressure in 2023.** External account balances have weakened substantially in 2022 given the absence of the usual Eurobond inflows, culminating in a drawdown of foreign currency reserves. A significant outflow of foreign portfolio investment, higher debt service obligation, and a slowdown in foreign direct investments dragged the Balance of Payments into a deficit equivalent to 5.1% of GDP (vs 2.1% surplus in 9M2021).

So far this year, foreign debt service amounted to USD 3.2bn while payments to Independent Power Producers (IPPs) is estimated at USD 800mn (Total: USD 4.0bn), depleting the forex reserves with pressure on the Ghanaian Cedi. By FY2022, the BOG anticipates an additional outflow of USD 800mn, emphasizing the unabating pressure on forex reserves with potential depreciation risk for the local currency.

The debt service-induced pressure on the forex reserves raises the necessity of a debt restructuring to reverse the downturn and restore exchange rate stability in 2023. Consequently, we expect a hard negotiation with non-resident investors and bilateral creditors to ease the external debt service burden in the short to medium term. Given the excess liquidity occasioned by the BOG's overdrafts to settle maturing domestic debt amidst the significant drawdown of foreign currency for external debt service, we foresee domestic and external debt restructuring as inevitable in 2023. This will be required to ease the debt service burden, preserve the forex reserves, anchor currency stability and support a decline in headline inflation.

**EVOLUTION OF INTERNATIONAL RESERVES**



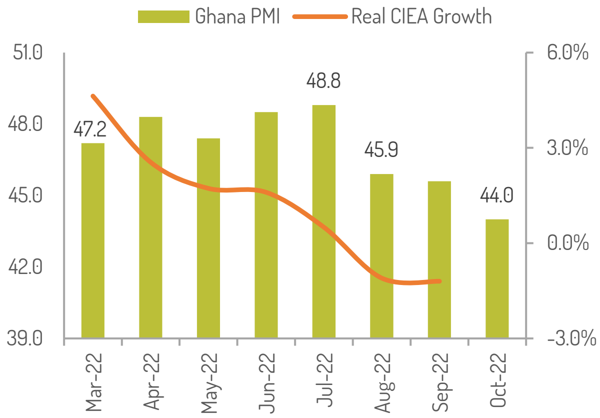

SOURCE: BANK OF GHANA

**The weakening economic activity will culminate in a lower real GDP growth in FY2023.** All indicators of economic activity continue to soften under the weight of the year-long currency depreciation and heightened cost of operation. The Purchasing Managers' Index (PMI) declined to 44.0pts in October 2022 (vs 51.8pts in December 2021), pointing to a sustained deterioration in business conditions in 2022.

High frequency data from the BOG's Composite Index of Economic Activity (CIEA) confirmed the ongoing weakening of economic activity. Specifically, cement sales have declined by c.18% YTD to 255,000 tonnes, highlighting downside risk for the construction sector. Similarly, container traffic at the ports also witnessed c.18% decline in the past 6-months, indicating downside risks to trade and commerce as FX shocks weigh on imports.

Against the backdrop of weakening economic activity and the business confidence index plummeting to 72.6pts in October 2022 (vs 98.4pts in December 2021), we forecast FY2022 real GDP growth at 3.4% with a further moderation to 2.7% by FY2023.

## REAL SECTOR INDICATORS




SOURCE: BANK OF GHANA, IHS MARKIT

**Banking sector remains profitable but risk to financial soundness is mounting.** Given the ongoing efforts of banks to reduce exposure to Government of Ghana securities amidst the uncertainty around debt restructuring, we continue to observe strong growth in the loan book. Total advances (GHS 81.2bn) grew by 57.5% y/y in October 2022 (vs 12.6% in December 2021) as bond redemptions are redirected into the loan book amidst the high interest rates. We note, however, that the sharp depreciation of the GHS in 2022 has contributed to the surge in the industry's loan book, supporting net interest margin.

However, average Capital Adequacy Ratio (CAR) plunged to 14.2% in October 2022, down from 19.6% at FY2021 and 1.2ppts above the prudential minimum of 13.0%. The decline in the average CAR was partly occasioned by the FX-induced surge in the loan book, which inflated the risk-weighted assets of banks to drag down the capital adequacy ratio. Also, the mark-to-market valuation of Treasury securities on the banks' balance sheet has resulted in significant capital erosion due to the plummet in bond prices this year.

At the current CAR level, we perceive a heightened solvency risk if the impending debt restructuring exerts significant stress on banks' capital. While the Bank of Ghana has assured of increased surveillance of the financial system to avert a distress event, we also believe the ongoing discussions for debt restructuring will be guided by the implications for solvency risk.

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