FUNDAMENTALS

GHANA'S MARCH INFLATION: MORE THAN A BASE EFFECT

13 APRIL 2023

Head, Insights
Courage Kingsley Martey
+233 240 970 832
Courage.martey@ic.africa

IN BRIEF

- Headline inflation declined more-than-expected to 45.0% y/y in March 2023 (-780bps) compared to the average market expectation of 50.2% (IC Insights: 49.7%).

- We believe the annual inflation for March 2023 partly reflects the benefit of a higher base effect from the food and energy price shocks occasioned by escalated geopolitical tensions and FX pressures from last year.

- Contrary to historical observation, the March 2023 CPI surprisingly contracted by 1.2% month-on-month, suggesting that the sharp decline in the headline inflation reflects more than just a favourable base effect. In our view, this could partly reflect the impact of demand destruction as the year-long price acceleration steadily weakens purchasing power and forces price reductions on items with a short shelf life.

- With the impact of the recent policy rate hike yet to filter to price developments, it appears the disinflation already found a tailwind as expected. This raises the possibility for the Bank of Ghana to take a breather on the rate hikes while observing the transmission of the last unexpected hike until the September 2023 MPC meeting.

- We expect the intensified pace of disinflation to cap the upside for yields on short-term securities while a potential IMF Board approval of Ghana's programme request in 2Q2023 revives the downward pressure. Although the 200bps hike in the Cash Reserve Ratio for local currency deposits (14.0%) could weaken investor demand for T-bills, a start of the IMF programme will reduce the Treasury's borrowing needs.

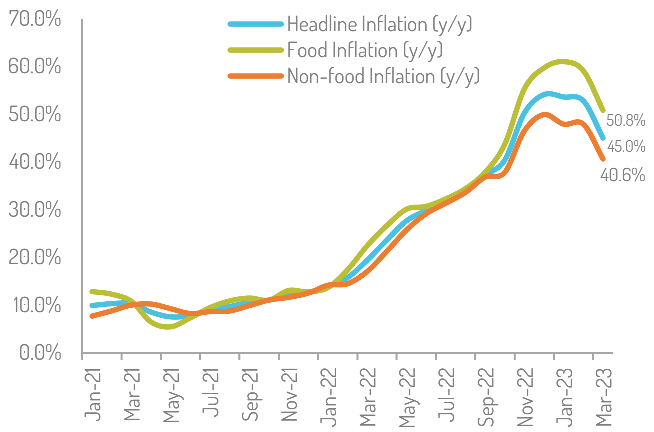
When the stars align

Ghana's annual inflation tumbled to a 5-month low in March 2023 as the stars aligned to cool the price pressures across food and non-food items. Headline inflation declined more-than-expected to 45.0% y/y in March 2023 (-780bps) compared to the average market expectation of 50.2% (IC Insights: 49.7%).

The decline in annual inflation was aided by a sharp fall in both food and non-food inflation. Food inflation nosedived 830bps to 50.8% y/y, mirroring a plunge in inflation for heavy weights such as ready-made food (55.1% y/y | -820bps), cereals (68.8% y/y | -700bps), and vegetable & tubbers (25.8% y/y | -800bps). Non-food inflation also slowed sharply by 730bps to 40.6% y/y, dragged down by lower inflation for transport (52.0% y/y | -1,830bps), utilities (64.7% y/y | -490bps), as well as clothing & footwear (38.3% y/y | -550bps).

On a broader scope, inflation for imported items also declined by 10.7pp to 51.6% y/y as the Ghanaian Cedi witnessed a slower depreciation during the Mar-2023 CPI data window to tame price pressures.

DISAGGREGATED CONSUMER PRICE INFLATION



SOURCE: GHANA STATISTICAL SERVICE

Sliding on a favourable base effect

We believe the annual inflation for March 2023 partly reflects the benefit of a higher base effect from the food and energy price shocks occasioned by escalated geopolitical tensions and FX pressures last year. On a year-on-year basis, we observed a slower rate of increase in Ghana's consumer price index (CPI) in 1Q2023 compared to the steep climb witnessed a year ago. These favourable base dynamics partly culminated in the lower year-on-year inflation of 45.0% in March 2023, which we expect will continue in the near-term. Within the context of a favourable base effect, the sharp drop in the headline inflation was largely expected.

............but this is more than a base effect

While we expected the onset of a favourable base effect to quicken the pace of disinflation from March 2023, we did not anticipate a month-on-month contraction in the CPI.

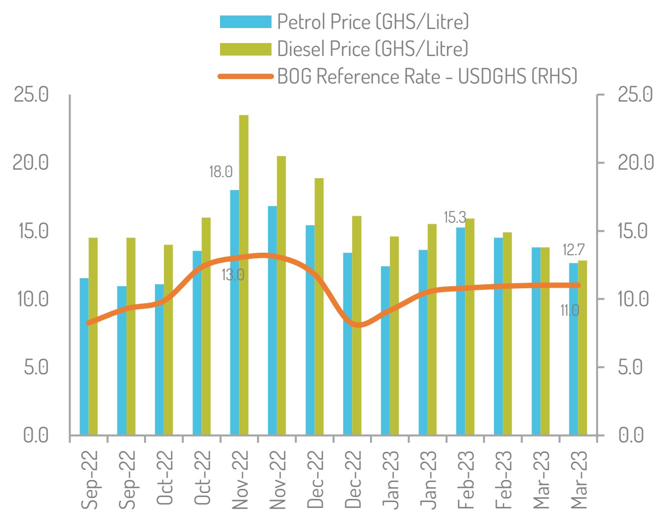
The overall CPI surprisingly contracted by 1.2% month-on-month, indicating a general fall in actual price levels ("deflation") between February 2023 and March 2023. Our analysis of Ghana's historical price developments showed that the CPI only contracts between August and October, underpinned by the impact of food harvest during the observed period.

However, in March 2023, the official CPI data recorded m/m deflation ("general price declines") for both food (-0.9% m/m) and non-food inflation (-1.5% m/m). In our view, this could partly reflect the impact of demand destruction as the year-long price acceleration steadily weakens purchasing power and forces price reductions on items with a short shelf life.

We also observed a sustained decline in domestic fuel prices over the past three consecutive pricing windows with a cumulative fall of 17.0% during the March 2023 CPI window. The lower energy prices contributed to the decline in transport and utility costs, respectively posting deflation rates of 4.0% m/m and 10.5% m/m in March 2023.

Consequently, we believe the unexpected month-on-month deflation in March 2023 suggests that the sharp decline in the headline inflation reflects more than just a favourable base effect.

EXCHANGE RATE AND PETROLEUM PRICE DYNAMICS



SOURCES: GHANA OIL COMPANY LIMITED, BANK OF GHANA, IC INSIGHTS

A reason to halt the policy rate hikes?

The sharper-than-expected decline in the March 2023 inflation revives the feeling that the Bank of Ghana may have been too hawkish with the 150bps hike in the policy rate to 29.5% at the March MPC meeting.

While the rate hike was unexpected by the market, the monetary authority indicated the need to "reinforce the pace of disinflation" as the basis for the hike. With the impact of the recent rate hike yet to filter to price developments, it appears the disinflation already found a tailwind as expected. This raises the possibility for the Bank of Ghana to take a breather on the rate increases while observing the transmission of the latest unexpected hike until the September 2023 MPC meeting.

Although the recent tax measures by the Ghanaian Treasury could elevate price expectations, we opine that the price effect will only slowdown the pace of disinflation rather than reverse the downward trend in y/y inflation. Against this backdrop, we maintain our FY2023 inflation forecast at between 22.7% – 24.7% with the expectation that the policy rate will remain unchanged at 29.5%, barring further shocks to energy, food and utility prices.

Yields for T-bills could find a resistance level around the 18.0% - 24.0% range

Following a sharp decline in early March 2023, yields for Ghanaian T-bills have found an upside impetus since late March as the unexpected policy rate hike offered support for short-term rates. Yields for the 91-day and the 182-day bills have gained 81bps each while the 364-day advanced by 129bps month-to-date.

However, we expect the intensified pace of disinflation to cap the upside for yields on short-term securities while a potential IMF Board approval of Ghana's programme request in 2Q2023 revives the downward pressure. Although the 200bps hike in the Cash Reserve Ratio for local currency deposits (14.0%) could weaken investor demand for T-bills, the IMF programme will reduce the Treasury's borrowing needs. This will offset the upside risk from a weaker demand and stabilize short-term yields along the 18.0% to 24.0% range in the near-term before a further decline by late 2023.

For more information contact your IC representative

Business development & client relations

Derrick Mensah
Head, Business Development
+233 24 415 5765
derrick.mensah@ic.africa

Dora Youri
Head, Wealth Management
+233 23 355 5366
dora.youri@ic.africa

Kelvin Quartey
Analyst, Business Development
+233 57 604 2802
kelvin.quartey@ic.africa

Corporate Access

Joanita Hotor
Corporate access
+233 50 137 6100
Joanita.hotor@ic.africa

Insights

Courage Kingsley Martey
Head, Insights
+233 240 970 832
courage.martey@ic.africa

Churchill Ogutu
Economist
+254 711 796 739
churchill.ogutu@ic.africa

Lydia Adzobu
Senior Analyst, Financial sector
+233 24 656 8669
Lydia.adzobu@ic.africa

Investing

Isaac Adomako Boamah
Chief Investment Officer
030 225 2623
isaac.boamah@ic.africa

Obed Odenteh
Portfolio Manager, Fixed Income
+233 54 707 3464
obed.odenteh@ic.africa

Timothy Schandorf
Portfolio Manager, Risk Assets
+233 24 292 2154
Timothy.schandorf@ic.africa

Herbert Dankyi
Analyst, Rates
+233 55 710 6971
herbert.dankyi@ic.africa

Clevert Boateng
Analyst, Consumer, Technology, Media & Telecommunication
+233 24 789 0452
clevert.boateng@ic.africa

Operations

Nana Amoa Ofori
Chief Operating Officer
+233 24 220 6265
nanaamoa.ofori@ic.africa

Emmanuel Amoah
Fund Administrator
+233 20 847 2245
emmanuel.amoah@ic.africa

Kelly Addai
Fund Accountant
+233 20 812 0994
kelly.addai@ic.africa

Trading

Randy Ackah-Mensah
Head, Global Markets
+233 24 332 6661
randy.amensah@ic.africa

Allen Anang
Equities,Trader
+233 54 084 8441
allen.anang@ic.africa

Isaac Avedzidah
Trader, Fixed Income
+233 24 507 7382
isaac.avedzidah@ic.africa