GHANA | MACROECONOMIC UPDATE | MONETARY POLICY | INSIGHTS

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FUNDAMENTALS

GHANA MPC UPDATE: BOLT FROM THE BLUE

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

IN BRIEF

- The Bank of Ghana delivered a surprise increase in the policy rate at the Mar-2023 MPC meeting, hiking the rate by 150bps to 29.5% in addition to a 200bps increase in the Cash Reserve Ratio on local currency deposits to 14.0%

- With the impending legislative approval of new tax measures, and the excess liquidity support to counter the shocks from the DDEP, we believe the authorities are mindful of upside risk to the downwardly sticky inflation rate. The Committee revised its end-2023 inflation forecast to 29.0%, up from the previous forecast of 25%, underscoring the need for a policy rate hike to re-align with the new 12-months outlook on inflation

- We estimate the 200bps hike in the CRR on local currency deposits to drain at least GHS 2.0bn from the interbank market. Consequently, we foresee moderation in appetite for T-bills as the lower yield on government securities pales into unattractive territory amidst the allure of 29.5% on the BOG bills. This will undermine the Treasury's capacity to meet its sizeable weekly auction targets while sustaining the aggressive yield suppression.

- Fiscal adjustment was strong in December 2022. However, we observed that the adjustment was solely driven by festivity-induced growth in revenue collection and the enforcement of tax compliance through retrospective tax liability assessments while the weak spending controls remain the fiscal Achilles heel.

An unexpected policy rate hike to 29.5%

The Bank of Ghana's Monetary Policy Committee (MPC) delivered a surprise increase in the policy rate at the Mar-2023 meeting, hiking the rate by 150bps to 29.5% (consensus forecast: 28.3% | IC Insights: 28.0%). Additionally, the MPC increased the Cash Reserve Ratio (CRR) on domestic currency deposits by 200bps to the Pre-Domestic Debt Exchange (DDE) level of 14.0% with effect from 13 April 2023.

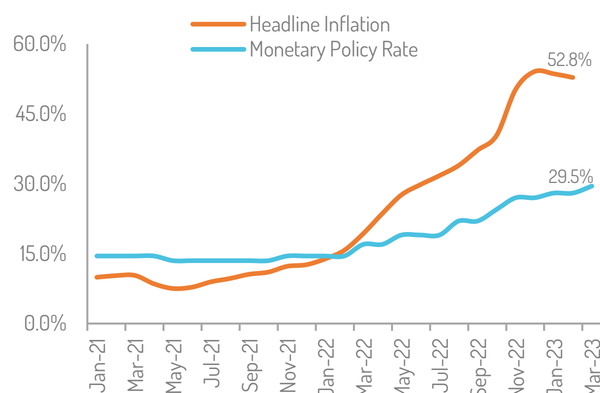
The Committee cited the need to reinforce the pace of disinflation and re-anchor inflation expectations towards the medium-term target of 8% ± 2% as current inflation remains above the desired level, despite recent declines.

Our views on the latest monetary policy decision

We believe the MPC is mindful of the potential upside risk to inflation arising from the impending legislative approval of some tax measures given that inflation has been downwardly sticky after peaking at 54.1% in Dec-2022. We also believe that the Bank of Ghana has assessed the impact of the DDE-related regulatory reliefs and ostensibly found excess liquidity than what the banks required, posing an upside risk to the inflation outlook.

The Committee revised its end-2023 inflation forecast to 29.0%, up from the previous forecast of 25%, underscoring the authorities' lingering concerns about inflation despite the easing price expectations. In view of the higher forecast inflation profile, we believe the BOG opted to revise the policy rate upward to re-align with the new 12-months outlook on inflation. We estimate that a more sluggish than expected pace of disinflation will open the window for a further 100bps hike by late 2023, although we expect the MPC to take a breather at this point.

INFLATION AND POLICY RATE PATH SINCE 2021



SOURCE: BANK OF GHANA, GHANA STATISTICAL SERVICE

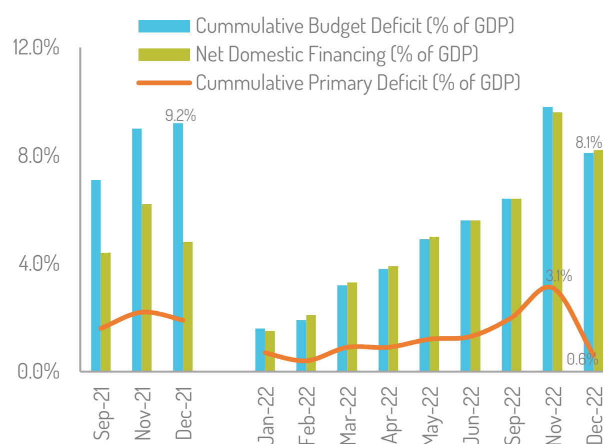
The weak spending controls remain a fiscal Achilles heel. Having announced the Domestic Debt Exchange Programme (DDEP) and secured a staff-level agreement with the IMF in Dec-2022, it appears the Treasury commenced a strong fiscal adjustment in the same month.

Notably, we observed a 2.5 percentage point m/m and 1.3 percentage point y/y fiscal adjustment as the primary budget deficit narrowed to 0.6% of GDP at FY2022. Although the primary deficit outturn remains worse than the FY2022 target surplus of 0.4%, the strong pace of adjustment in a single month gives us a hopeful feeling for FY2023, subject to an IMF-supported programme.

The overall budget deficit also narrowed by 1.7 percentage point m/m and 1.1 percentage point y/y to close 2022 at 8.1% of GDP, albeit above the revised FY2022 target of 6.3%.

We observed that the adjustment was solely driven by festivity-induced growth in revenue collection and the enforcement of tax compliance through retrospective tax liability assessments. While total revenue (GHS 96.7bn | 15.7% of GDP) was broadly in line with the revised target, the authorities were unable to rein-in public spending. Total expenditure stood at GHS 146.3bn at FY2022, exceeding the budget limit by 7.8%. The authorities' difficulties with keeping a lid on expenditure continues to cast doubt on any credible fiscal plan without an IMF programme.

EVOLUTION OF THE BUDGET DEFICIT AND FINANCING



SOURCE: BANK OF GHANA

Contraction in import volumes and suspension of external debt service helps to stabilize the forex cover. On the external accounts, export revenue commenced 2023 on a strong note, growing by 9.5% y/y to USD 2.8bn as of Feb-2023. The rise in export revenue was supported by a 35.8% y/y surge in gold

receipts (USD 1.1bn) which outweighed the 18.3% decline in oil revenue (USD 562.6mn) in the first 2-months of the year.

Additionally, import bills fell by 11.8% y/y to USD 2.0bn as the value of non-oil imports contracted by 17.6% y/y to USD 1.4bn as of Feb-2023. This resulted in a 266% y/y improvement in Ghana's trade surplus to USD 752.8mn (1.0% of GDP).

We attribute the fall in Ghana's import bill and the resultant surge in the trade surplus largely to a volume contraction in imports during the first 2-months of the year. An analysis of the gross forex reserves showed a 5.0% decline in the first 2-months to USD 5.9bn. However, the lower gross forex reserve showed a slightly improved import cover of 2.8 months as of Feb-2023 (vs 2.7 months at FY2022). We believe this reflects a fall in import volumes, which ostensibly began in Nov-2022 as the Central Bank stopped the sale of FX to importers of "non-essential items". Consequently, we infer that the 17.6% y/y decline in the value of non-oil imports reflects the impact of volume contraction rather than an easing of prices on Ghana's non-oil imports.

The authorities' decision, in Dec-2022, to suspend servicing most of its external debt has also helped to limit the attrition in Ghana's forex reserves, helping to stabilize FX supply in 1Q2023.

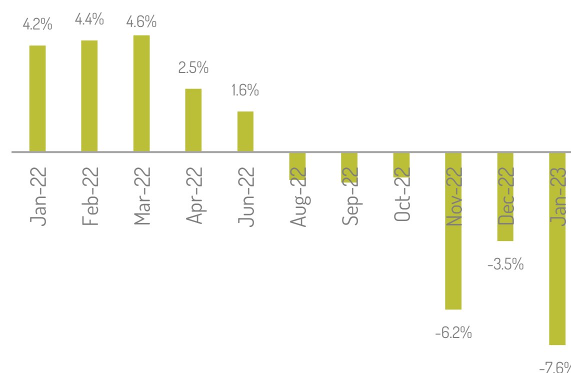
Economic growth will bear the brunt of lower non-oil imports and fiscal adjustments in 2023. Although we view the decline in imports and the resultant widening of Ghana's trade surplus as favourable for the country's balance of payments position, we foresee a negative spill over to the real sector in 2023.

The decline in non-oil import volumes could negatively impact the trades, manufacturing, and construction sectors. Our review of the Bank of Ghana's high frequency data showed ≃20% y/y fall in container traffic at the Ports and ≃28% y/y decline in cement sales as of Jan-2023. Consequently, the real Composite Index of Economic Activity (CIEA) contracted by 7.6% y/y in Jan-2023 compared to a 4.2% expansion in the same period 2022.

Additionally, the necessity of fiscal adjustments in 2023 is fuelling the government's revenue drive with new revenue Bills under legislative consideration for approval. We expect these levies to increase the cost of sales for businesses and weigh on the purchasing power of consumers, ultimately constraining economic activity in 2023.

In view of the weakening economic activity, we reiterate our real GDP growth forecast range of between 2.2% – 3.2% for FY2023 (GOG: 2.8%).

REAL COMPOSITE INDEX OF ECONOMIC ACTIVITY GROWTH



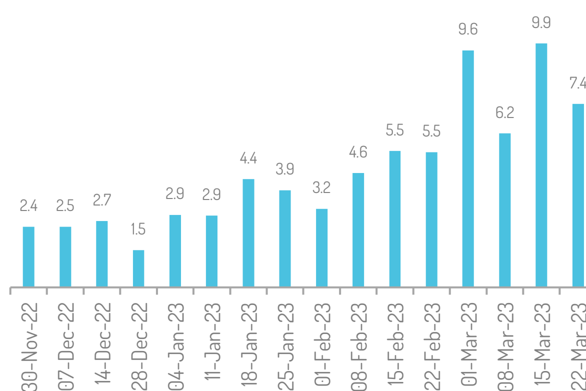
SOURCE: BANK OF GHANA

The latest monetary stance could stifle demand for T-bills. We estimate the 200bps hike in the CRR on local currency deposit to drain at least GHS 2.0bn from the interbank market and weigh on demand for the relatively lower-yielding T-bills.

Our analysis of interbank liquidity conditions revealed a surge in GHS liquidity after the DDEP-induced reduction in CRR to 12%. The average weekly interbank liquidity mopped up by BOG bills increased by 142% to GHS 5.5bn after the CRR reduction, with the March 2023 average mop ups hitting GHS 8.3bn. While we expect the CRR hike to tighten liquidity by at least GHS 2.0bn, we believe commercial banks will calibrate fund placements in favour of the BOG bills given its higher yield at the new policy rate of 29.5%.

Consequently, we foresee moderation in appetite for T-bills as the lower yields on government securities pales into unattractive territory amidst the allure of 29.5% on the BOG bills. This will undermine the Treasury's capacity to meet its sizeable weekly auction targets while sustaining the aggressive yield suppression. Ultimately, we expect yields for T-bills to find a floor along the 15.0% – 19.0% range in 2023.

WEEKLY DEMAND FOR BOG BILLS (GHS bn)



SOURCE: BANK OF GHANA

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

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