FUNDAMENTALS

READYING FOR POLICY PIVOT

GHANA MACROECONOMIC OUTLOOK 2024

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IN BRIEF

How we fared in 2023

- The 2023 policy framework in Ghana aimed at restoring macroeconomic stability with a tightly complementary fiscal and monetary stance under a 3-year IMF-supported reforms agenda. Against this backdrop, the policy rate and interest rates on T-bills remained generally sticky around the 30.0% handle while the low-coupon restructured Treasury bonds struggled for price discovery and liquidity.

- The Ghanaian Stock Exchange (GSE) outperformed expectations with a year-to-date gain of 29.7% on the composite index as of end-November 2023. The GSE financial stock index (GSE-FSI) bottomed-out in August 2023, pivoting upwards to post a 20.4% gain in the 3-months to end-November 2023. Given the dearth of activity in the bond market, pension funds increased their stock market participation, accounting for 17.0% (GHS 196.3mn | +23.0% y/y) of value traded on the stock market in 10-months of 2023 (vs 6.0% in the same period of 2022).

What we see ahead in 2024

- Inflation will continue its downturn in 2024, but with a non-linear trend while the prevailing tight monetary stance and the ongoing IMF programme act as key policy anchors. We anticipate an upside detour in March 2024, mainly due to unfavourable base drift effect given the unexpected decline in the CPI level in March 2023. Against the counteracting forces to inflation in 2024, we project Ghana's FY2024 annual headline inflation at 16.1% ±1.0pp (vs GOG Target: 15.0%).

- The Ghanaian Cedi will benefit from a dovish US FED and the recent monetary policy decisions on banks' Cash Reserve Ratio but the weak forex reserve will leave the local currency vulnerable. The authorities' target to achieve an improved cover of 1.7 months of imports gives us little comfort about the shock-absorbing capacity of external buffers. We expect the potential safe-haven demand for forex, associated with election-related uncertainty, to exert a modest depreciation pressure on the Ghanaian Cedi given the constrained intervention capacity of the Central Bank.

- Our downside view on inflation in 2024 creates a pathway for nominal yields on T-bills to decline amidst monetary policy pivot to an easing bias in the coming year. However, we opine that the pace of yield compression in 2024 will be determined by a number of factors including the pace of disinflation, the risk to FX stability with resultant policy rate positioning, and the public sector domestic borrowing requirements.

How we fared in 2023

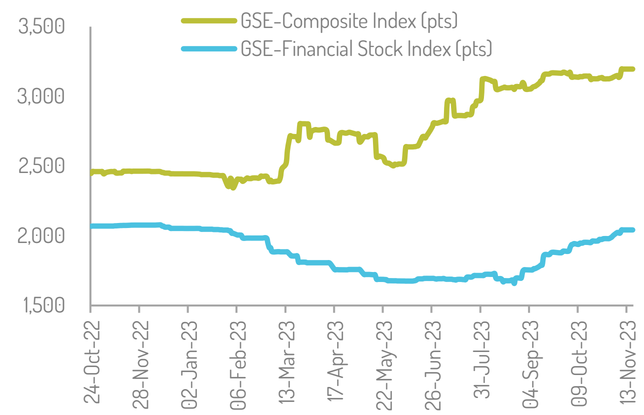
The GSE climbed a wall of worry, while bond market laid comatose amidst tighter policy environment

The 2023 policy framework in Ghana aimed at restoring macroeconomic stability with a tightly complementary fiscal and monetary stance under a 3-year IMF-supported reforms agenda.

While 2023 inflation cumulatively declined by 18.9pp to 35.2% as of October 2023, price pressures remained evidently high with headline inflation at over 3x the medium-term upper target of 10.0%. The early-year stickiness, largely due to taxes, utility tariffs, FX, and food price hikes, empowered the Bank of Ghana's continued hawkish policy stance to push the terminal policy rate to a record 30.0%.

Against this backdrop, interest rates on Treasury bills remained generally sticky around the 30.0% handle while the low-coupon restructured Treasury bonds struggled for price discovery and liquidity. Trading activity on the secondary bond market was further hampered by the restructuring-induced fragmentation of the bond market as pension funds held a differently structured bond from those of commercial banks, and mutual funds.

PERFORMANCE OF THE GHANAIAN STOCK MARKET IN 2023



SOURCE: BANK OF GHANA, GHANA STATISTICAL SERVICE

Despite the challenging macroeconomic backdrop and the 60.0% y/y drop in trade volume, the Ghanaian stock exchange (GSE) outperformed expectations with a year-to-date gain of 29.7% on the composite index as of end-November 2023. The financial stock index (GSE-FSI) bottomed-out in August 2023, pivoting upwards to post a 20.4% gain in the 3-months to end-November 2023. While the macroeconomic challenges lingered in the background, we believe the start of the USD 3.0bn IMF-supported programme reignited selective risk-taking amidst impressive 9M2023 financial results, with MTNGH driving market activity. Given the dearth of activity in the bond market, pension funds increased their stock market participation, accounting for 17.0% (GHS 196.3mn | +23.0% y/y) of value traded on the stock market in 10-months of 2023 (vs 6.0% in the same period of 2022).

What we see ahead in 2024

Improving macroeconomic condition will be clouded by election-related uncertainty

The ongoing 3-year IMF-supported reforms programme will anchor the policy environment and sustain the steadily improving macroeconomic conditions in 2024. The front-loaded nature of fiscal adjustment in FY2023 provides room to soften the pace of adjustment in 2024, slightly easing the constraint to growth in the year ahead.

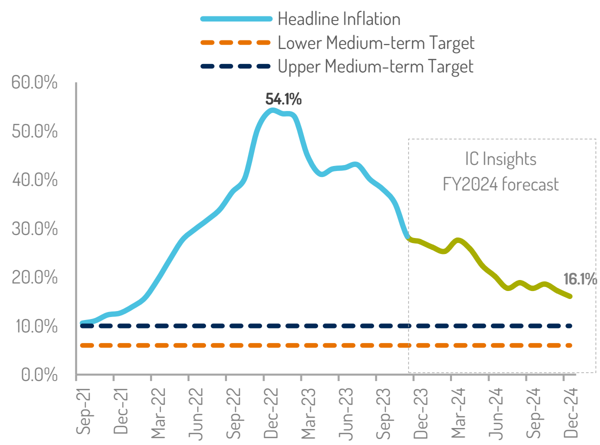
However, election years have generally been the Achilles heel of fiscal sustainability in Ghana. In view of this, we are mindful of the potential macroeconomic effects and safe-haven positioning as Ghana's 2024 general elections approach (Election date: 07 December 2024).

Inflation will continue its downturn, with a non-linear trend. The pace of disinflation expectedly quickened in 2H2023, helped by favourable base effect, moderation in food price pressures, diminishing impact of earlier tax hikes and post-January 2023 slowdown in the Cedi's depreciation. We also attribute the disinflation trend to the appropriately tight monetary policy stance, which includes the elimination of Central Bank financing of the Treasury's budget deficit.

Having declined cumulatively by 18.9pp to 35.2% in October 2023, we expect headline inflation to outperform the authorities' upper target of 31.4% and central target of 29.4%, potentially closing FY2023 at 27.3% ± 1.0pp.

In 2024, we expect the declining momentum to continue with the prevailing tight monetary stance and the ongoing IMF programme as key policy anchors. However, we anticipate an upside detour in March 2024, mainly due to unfavourable base drift effect given the unexpected decline in the CPI level in March 2023. From May to July 2024, we anticipate favourable base effect to set in and outweigh the seasonal food price shocks, exerting downward pressure on headline inflation into 2H2023

HISTORICAL AND PROJECTED PATH OF INFLATION



SOURCE: BANK OF GHANA, GHANA STATISTICAL SERVICE, IC INSIGHTS

However, upside risk could intensify ahead of the elections in December 2024 as heightened uncertainty potentially fuels safe-haven demand for foreign currency, with a pass-through of depreciation pressure to inflation. Geopolitical risks in the Middle East and Eastern Europe together with output cuts by OPEC+ in response to weaker global demand could revive upward pressure on energy prices. This will spill over into domestic energy prices and utility tariffs with upside risk to inflation in 2024.

Against the counteracting forces to inflation in 2024, we project Ghana's FY2024 annual headline inflation at 16.1% ±1.0pp (vs GOG Target: 15.0%)

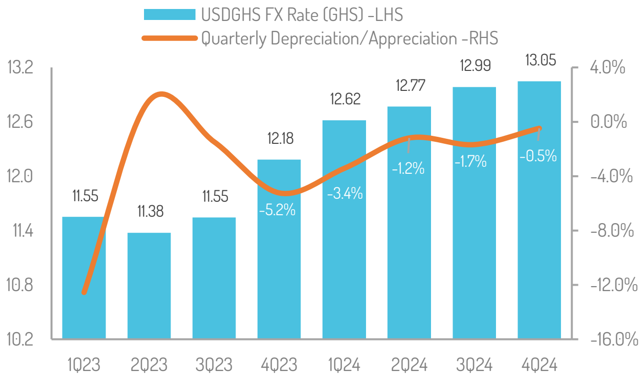
The Ghanaian Cedi will benefit from a dovish US FED but the weak forex reserve will leave the local currency vulnerable. The latest US real sector indicators are pointing to a softening momentum in economic activity in the coming year, prompting global market investors to price-in rate cuts in 2024. Investors currently expect at least a 25bps rate cut at the June 2023 FOMC meeting (with a 79.1% probability of occurrence). This dovish tilt in market sentiment weighed on US Dollar strength as the Dollar Index (DXY) fell to 103.5pts as of end-November 2023 (vs 106.9pts at end-October 2023). We view the dovish outlook for US monetary policy as favourable for risk assets, including the Ghanaian Cedi in 2024.

On the domestic front, we expect the prevailing IMF-supported policy environment to anchor the Cedi's performance. The ongoing disinflation and the latest hike in Cash Reserve Ratio to 15.0% with a directive for banks to keep cash reserve on foreign currency deposits in Cedis will incentivise Cedi-biased positions in asset allocation. While the potential resumption of external debt service in 2024 could revive depreciation pressure, we expect the programme-related inflows from multilateral sources to fund the restart of modest external debt service.

Notwithstanding the aforementioned supportive factors, the Cedi remains susceptible to unexpected domestic and external shocks, in our opinion. Gross forex reserves (excl. encumbered assets and petroleum funds) stood at USD 2.5bn (1.1 month of import cover) as of October 2023. The authorities' target to achieve an improved cover of 1.7 months of import by end-2024 gives us little comfort about the shock-absorbing capacity of external buffers. We expect the potential safe-haven demand for forex, associated with election-related uncertainty, to exert some depreciation pressure on the Ghanaian Cedi given the constrained intervention capacity of the Central Bank.

Also, we estimate that a worse-than-expected outcome on external debt restructuring negotiations would elevate FX uncertainty and depreciation pressure in 2024. Consequently, we forecast FY2024 USDGHS at 13.1/USD ±GHS 0.1 (Depreciation: 6.6% ±0.7pp), albeit a modest depreciation compared to FY2023.

HISTORICAL AND PROJECTED EXCHANGE RATE PATH



SOURCE: BLOOMBERG, IC INSIGHTS

Election-induced spending will revive growth modestly but the general private sector pulse will remain weak. With our expectation that real GDP growth will bottom-out in 2023 at 2.4%, a less aggressive fiscal squeeze in 2024 on account of election-induced spendings will provide a catalyst for modest rebound in growth.

After the frontloaded adjustment in 2023, we expect fiscal policy to pivot in the direction of softer correction in the fiscal imbalance in 2024 without compromising the IMF's performance criteria. In the 2024 budget, the Ghanaian authorities signalled a target fiscal adjustment of 1.0% of GDP, a softer pace compared to the 3.8% adjustment implemented in 2023. Subject to improved revenue outturn, this gives room for the authorities to execute the strong CAPEX plan of GHS 28.7bn (+54.3% y/y).

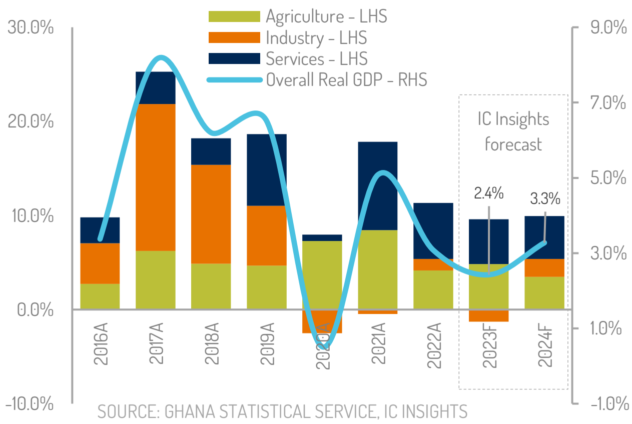
The upscaling of public investment will stimulate a rebound in the construction sector, which contracted for four straight quarters as of 1H2023. We also perceive the benefit of a favourable base effect to growth in the construction sector following the successive quarters of shrinkage. However, a disappointing fiscal revenue performance will restrain the public investment drive and cap the anticipated recovery. We expect the manufacturing sector to benefit from moderating producer and consumer price pressures, partly reviving idle capacity in 2024 after four consecutive quarters of contraction as of 1H2023. The industry sector will receive further boost from new oil wells under the ongoing Jubilee South East (JSE) project to push oil output from the Jubilee field above 100,000 barrels per day. We, however, perceive downside risk from the Tweneboa Enyenra Notmme (TEN) oil field as under-investment culminates in natural field decline while continued re-injection of gas in the Jubilee and Sankofa fields remains a lingering concern.

We expect momentum in the agriculture sector to cool in 2024, on the back of disappointing cocoa production in the ongoing 2023/24 crop season which extends to end-September 2024.

In the services sector, we are bullish on the growth outlook for information & communication, transport & haulage, as well as the public sector-influenced segments such as education, public administration, and health sub-sectors. We also expect lower inflationary pressures and a more stable exchange rate to support recovery in the trades sub-sector, which also endured two straight quarters of contraction in 1H2023. However, we are less optimistic about the outlook for finance and insurance activities as subdued fixed-income trading and the likely focus on banks' recapitalisation will undermine near-term risk appetite amidst election year uncertainties.

In view of the foregoing, we project FY2024 overall real GDP growth at 3.3% ±0.5pp (vs GOG target: 2.8%).

HISTORICAL AND FORECAST REAL GDP GROWTH



SOURCE: GHANA STATISTICAL SERVICE, IC INSIGHTS

Yields on T-bills will fall, but the Treasury's high borrowing pressure will create some downward stickiness. Our downside view on inflation in 2024 creates a pathway for nominal yields on Treasury bills to decline amidst a policy pivot in the coming year. However, we opine that the pace of yield compression in 2024 will be determined by a number of factors including the pace of disinflation, the risk to FX stability with resultant policy rate positioning, and the public sector domestic borrowing needs.

The target financing of GHS 61.9bn (5.9% of GDP) overall budget deficit solely with T-bill issuances, in addition to the upcoming T-bill maturities, signals higher gross public sector borrowing need in 2024. If we assume the Treasury's plan to build a buffer of GHS 31.8bn (3.0% of GDP) will emerge from excess uptakes at the weekly auctions, this will further elevate the borrowing pressure on T-bills. Consequently, we foresee the high domestic borrowing pressure partly mitigating the pace of expected decline in yields for T-bills in 2024.

Having peaked at 30.0% in 2023, we expect monetary policy to pivot in the direction of policy rate cuts after inflation sufficiently declines to restore a positive and restrictive real policy rate. In view of this, we anticipate a cautious downward path for the policy rate in 2024, with a first cut potentially in May 2024. We foresee potential seasonal FX pressure in 1Q2024 as well as election-related and external debt restructuring uncertainties as the likely restraints on the pace of monetary easing in 2024. Against this backdrop, yields for T-bills will also decline cautiously in lockstep with the policy rate path in 2024.

Our inflation forecast suggests an average inflation of 24.6% in 1H2024, with a moderation in the average inflation to 17.7% in 2H2024 (year-end: 16.1% ±1.0pp). We think investors will demand positive real returns of between 3.0% – 6.0% in 2024, after booking negative real returns since 2022. This should bring the average nominal T-bill interest rates to between 27.6% – 30.6% in 1H2024, and a further decline in the average yields to between 20.7% – 23.7% in 2H2024.

On the domestic bond market, we anticipate a quiet year ahead as the Treasury signalled the absence of new issuances while the existing restructured bonds struggle for price discovery and liquidity. We expect Repurchase Agreements and "Sell-buybacks" to dominate any deals in the restructured bonds in 2024.

Restating the key risks to watch

- **Election-induced uncertainty:** Ghana's Presidential and Parliamentary elections have typically birthed policy and macroeconomic uncertainty, especially with incumbents at the end of their second term. The election-induced uncertainty will weaken appetite for medium-term investment decisions, heightening the appeal of short-term and safe-haven assets.
- **Geopolitics:** The ongoing Russia-Ukraine war and the recently escalated Israel-Hamas conflict are the global geopolitical hotspots we see extending into 2024. The main transmission conduits will be via energy prices, exchange rate, inflation, and interest rates, especially if the Middle East war spills over to actively involve Iran. The less-talked-about US-China decoupling has intensified in recent months with negative risks to global trade, supply chains, and investment flows.
- **External debt restructuring outcome:** The IMF expects the ongoing negotiations to restructure Ghana's external debt to deliver estimated savings of USD 2.2bn on external debt service in 2024. A less favourable outcome could heighten the FX pressure beyond our baseline expectation, limiting the downside scope for inflation and interest rates.
- **IMF quota increase bodes well.** In November 2023, the IMF Executive Board proposed a 50% increase in quota contributions by member countries. While we do not view this proposal, when approved, as an automatic increase in disbursement to Ghana, we think it provides an opportunity to upscale the size of the ongoing ECF programme to mitigate unexpected external shocks.

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