Clarity in the Chaos:

What Lies Ahead for the Ghanaian Economy

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HIGHLIGHTS

- Recent years have presented significant economic challenges for Ghanaian households and businesses.
- We maintain a cautiously optimistic outlook for the Ghanaian economy's near-term future.
- There is a feasible path to achieving public debt sustainability, though it may significantly impact households and businesses.
- We strongly recommend the incoming government to review the price stability mandate of the Bank of Ghana
- Our analysis finds insufficient evidence to claim superior economic performance under either the NPP or NDC regimes.

REVIEW OF THE GHANAIAN ECONOMY

The Ghanaian economy has faced significant challenges over the past two years, marking a period of considerable economic strain. These challenges have been manifold, encompassing sluggish economic growth, rampant unemployment, soaring inflation rates, sharp depreciation of the currency, a decline in gross international reserves, and a severe public debt crisis. This section aims to dissect the economic landscape of Ghana by meticulously analyzing the performance of key macroeconomic indicators during 2022 and 2023. Our approach involves a detailed comparison of recent data against the five-year average preceding the peak of the crisis (2017-2021), offering a historical perspective on the economic downturn. Furthermore, we juxtapose these outcomes with the anticipated long-term targets, which represent the benchmarks an economy would typically aim for when operating at or near its full potential. Through this comprehensive analysis, we seek to shed light on the extent of the economic challenges faced by Ghana and evaluate the effectiveness of measures implemented to navigate this tumultuous period.

Table 1: Performance of Key Macroeconomic Variables

Key Macroeconomic Variables	5-year Average (2017 -2021)	2022	2023	Long Run target
Real GDP Growth Rate(%)	5.29	3.1	2.3	5
Inflation Rate(%)	10.4	54.1	23.2	8
Cedi Depreciation(%)	6.8	30	27.8	6
Public debt-to-GDP Ratio (%)	65.8	93.3	69.0	60
Gross International Reserve	4.1	0.7	1.1	4
Policy Rate (%)	16.4	27	30	13

Sources: Bank of Ghana, Ministry of Finance, IMF, Authors calculations

Real GDP growth rates for 2022 and 2023 stood at 3.1% and 2.3%, respectively. These figures fell short of the 5.29% average growth experienced from 2017 to 2021 and were below the 5% potential growth rate projected by our forecast model. Previously, the growth was primarily fueled by the service industry, non-extractive sectors, and agriculture. However, while agriculture continued to contribute positively to GDP growth in 2022 and 2023, the service industry saw a significant decrease in its growth contribution. Furthermore, the non-extractive industry experienced a downturn, contributing negatively to growth, likely due to reductions in public investment.

The economic landscape in 2022 and 2023 was further characterized by significant challenges across other key macroeconomic variables, as illustrated by the data in

Table 1. The inflation rate surged to 54.1% in 2022 and remained high at 23.2% in 2023, dramatically exceeding the five-year average of 10.4% and far outpacing Bank of Ghana's policy target of 8%. This inflationary pressure observed in Ghana was broad based and could be observed across all 13 divisions of the CPI basket, exacerbated by external and internal shocks.

The depreciation of the Cedi against the USD was significant, with the rates hitting 30% in 2022 and 27.8% in 2023. These figures sharply diverge from the previous five-year average depreciation rate of 6.8%, and significantly exceed the long-term target of 6%. Such depreciation rates were unexpected, especially when considering the policy goals of Ghana and the US. Ideally, if both economies were functioning optimally and achieving their respective inflation targets—8% for Ghana and 2% for the US—the theory of Purchasing Power Parity (PPP) suggests that the Cedi should depreciate by only 6%. This marked depreciation not only underscored the vulnerabilities in the currency market but also signaled a notable decline in investor confidence and large capital outflows, particularly following Ghana's loss of market access in 2022.

Public debt sustainability became a more pressing concern, with the public debt-to-GDP ratio escalating to 93.3% in 2022 and slightly improving to 86.1% in 2023. Both figures substantially exceed the five-year average of 65.8% and the debt sustainability target of 60%. The gross international reserves experienced a significant decline, providing only 0.7 months of import cover in 2022 and marginally better coverage of 1.1 months in 2023, compared to a more robust five-year average of 4.1 months and the IMF LIC reserve adequate metric of 4 months import cover. This decline in reserves underscores the country's diminishing buffer against external shocks, making it more vulnerable to global financial volatilities.

Lastly, the policy rate saw an upward trend, reaching 27% in 2022 and further increasing to 30% in 2023, markedly higher than the five-year average of 16.4%. The Bank of Ghana tightened monetary policy through in an increase of the policy rate by a cumulative 1500 basis points in 2022 and followed by an additional increase of 50 basis points early in 2023. This surge in the policy rate, which far exceeds the target of 13% suggested by our model, reflects the central bank's assertive efforts to combat inflation. However, this aggressive monetary tightening could potentially hinder economic growth by raising the cost of borrowing.

GHANA’S ECONOMY OUTLOOK

In light of the challenges faced by the Ghanaian economy over the past two years, as highlighted in the previous sections, this section aims to provide an insight into the economic outlook for Ghana in 2024 and 2025. Despite the hurdles, there is a cautious optimism regarding the near-term prospects of the Ghanaian economy. While a full recovery to its long-term potential is not anticipated immediately, it is expected that the key macroeconomic indicators will stabilize and, in some areas, show significant improvement from the troughs experienced in 2022 and 2023.

This optimistic outlook is grounded in a few pivotal factors. First, a favorable shift in global monetary conditions is expected to alleviate some external pressures. Secondly, domestic fiscal consolidation efforts are projected to stabilize and strengthen the economy's foundation. Lastly, the support from the International Monetary Fund (IMF) through the Extended Credit Facility (ECF) program is anticipated to provide a structured path for economic recovery and stability.

However, despite these positive indicators, it's important to approach this outlook with caution. There are still considerable risks that could potentially derail the economic recovery process. These risks include volatile global economic conditions, potential fluctuations in commodity prices, delays in restructuring external debt, and domestic challenges such as political instability , particularly with the upcoming elections or delays in implementing structural reforms under ECF program. Thus, while there is a basis for optimism, vigilance and adaptive policy responses will be crucial in navigating the uncertainties that lie ahead for the Ghanaian economy in 2024 and beyond.

Table 2: Forecast of Key Macroeconomic Variables

Key Macroeconomic Variables	2023	2024	2025
Real GDP Growth Rate(%)	2.3	2.8	4.4
Inflation Rate(%)	23,2	17	10
Cedi Depreciation(%)	27.,8	14	8
Public debt-to-GDP Ratio (%)	69.0	67.1	64.1
Gross International Reserve	1.1	1.7	2.4
Policy Rate (%)	30.4	25	17

Table 2 summarizes our forecast for key macroeconomic variables. The projections indicate a positive trajectory for the Ghanaian economy, with several notable developments expected. Output is expected to pick up from 2023 and further increase to 4.4% in 2025. The disinflationary trend that began in 2023 is expected to persist, with the inflation rate decreasing to 17% in 2024 and a further decrease to 10% in 2025, aligning with the Bank of Ghana's target. This downward trend in inflation is likely to prompt the Bank of Ghana to cut its policy rate by 500 basis points in 2024, reaching 17% by the end of 2025.

Despite expectations for the cedi to be more stable than in recent years, we foresee a depreciation of 14% in 2024 and 8% in 2025. This depreciation may be more pronounced due to the Bank of Ghana's anticipated rate cuts and the slower-than-expected easing of monetary policy by major central banks, such as the US Federal Reserve. Moreover, a debt payment moratorium agreed with official creditors, lasting until May 2026, is expected to significantly aid in rebuilding Ghana's international reserves, which are projected to cover 1.7 and 2.4 months of imports in 2024 and 2025, respectively.

DEBT SUSTAINABILITY ANALYSIS

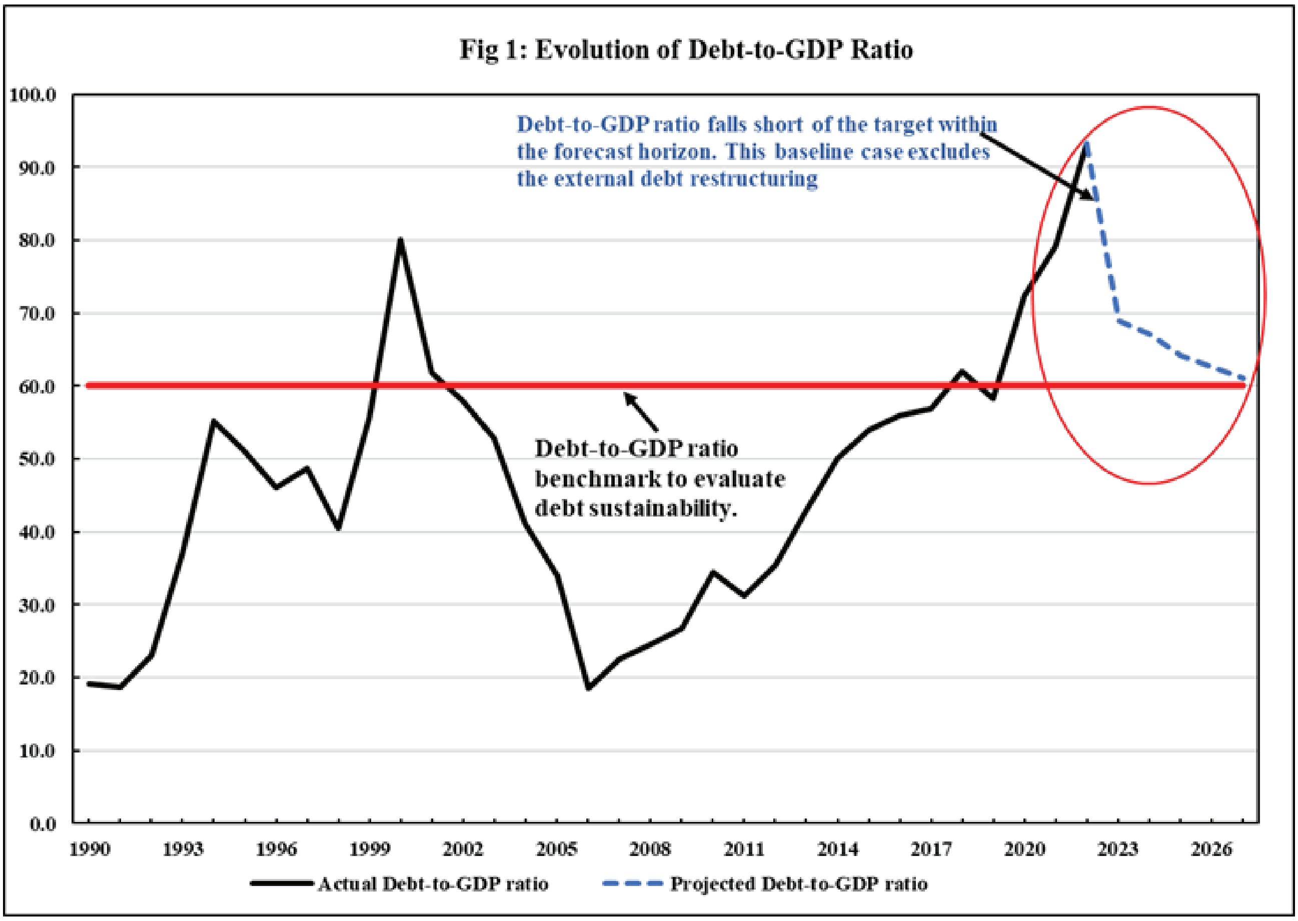
At the core of Ghana's economic troubles lies a critical public debt issue. This crisis, while exacerbated by the structural frailties of the economy, was significantly intensified by external shocks from the COVID-19 pandemic and the fallout from the Russia-Ukraine conflict. However, the tipping point was the fiscal authorities' inability to fulfill debt obligations. The situation worsened when Ghana lost access to international markets in late 2021, resulting in a plummeting of investor confidence and substantial depletion of international reserves. Thus, it is essential that any strategies to regain macroeconomic stability prioritize public debt sustainability and the restoration of market access. In response, Ghana sought the IMF's support in July 2022 and initiated a comprehensive debt restructuring program, addressing both domestic and external debts. The restructuring of domestic debt is complete, though negotiations with external creditors are ongoing. Specifically, we scrutinize the government's strategy, as detailed in the 2024 Budget, to manage debt sustainably. We also evaluate the contribution of each strategy to the overarching goal of ensuring public debt sustainability over the forecast period.

In 2022, Ghana's total public debt reached GHS 563.7 billion, accounting for 93.3% of its Gross Domestic Product (GDP). This figure was forecasted to slightly increase to GHS 589.4 billion by the end of 2023, but due to GDP growth, the debt-to-GDP ratio is expected to significantly drop to 69.0%. In our analysis, we aim for a public debt-to-GDP ratio of 60%, which aligns with the IMF's benchmark; commonly used to evaluate the debt sustainability. Through the medium-term goals specified in the 2024 budget, we will examine the trajectory of Ghana's public debt in relation to this 60% threshold.

The following are the major medium-term targets outlined in the 2024 budget:

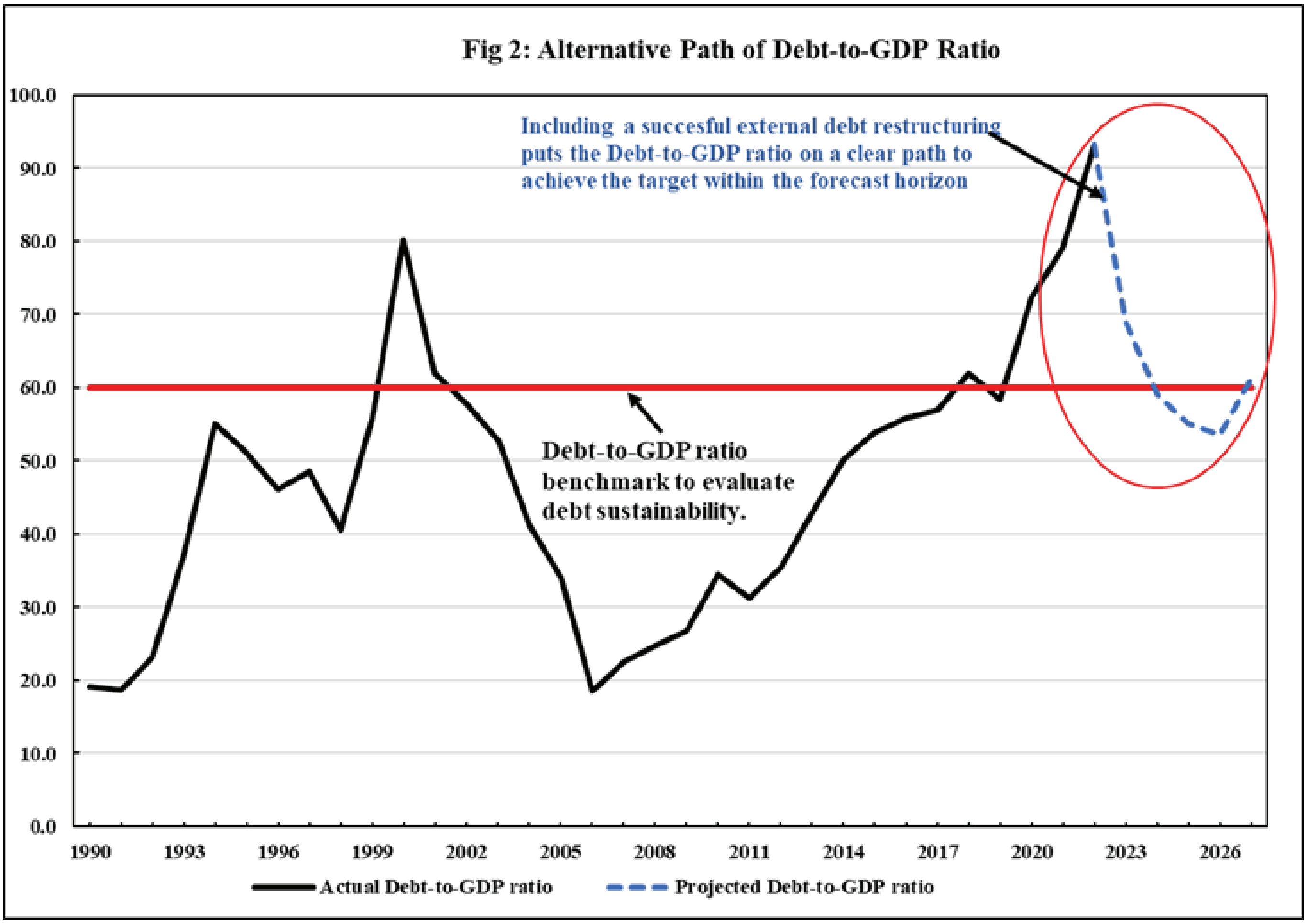
- Overall Real GDP to grow at an average of 2.8%
- End-December inflation rate of 15.0%
- Primary Balance on Commitment basis at a surplus of 0.5% of GDP
- Gross Internation Reserve to cover not less than 3.0 months of import cover.

A representative threshold of a public debt to GDP ratio of 60% is used to indicate high debt level. Under very simplifying assumptions including the interest rate on the debt is expected to be lower than the growth rate of GDP over the time horizon, a 60% nominal debt to GDP ratio can be equivalent to 55% PV of debt-to-GDP ratio which is the advertised target by the government.



Sources: Bank of Ghana, Ministry of Finance, IMF, Authors calculations

Our projection in Fig 1 shows that under the baseline scenario, the debt-to-GDP ratio does not meet the desired target throughout the forecast period. This scenario takes into account the government's policies for 2023, including the Domestic Debt Exchange Programme (DDEP) and the goals set in the 2024 budget, but it does not factor in the ongoing negotiations for external debt restructuring. Given that the government is in talks to secure approximately $10.5 billion in financing over our forecast period, we analyzed the potential impact on the public debt-to-GDP ratio assuming a successful external debt restructuring. Success in this context would mean the government achieving 80% subscription. Fig 2 illustrates that achieving debt sustainability is possible with the successful conclusion of these external debt restructuring negotiations.



Sources: Bank of Ghana, Ministry of Finance, IMF, Authors calculations

Recognizing a viable route to restoring debt sustainability, we will assess the effectiveness of various strategies aimed at bringing public debt back to manageable levels, along with their impact on Ghanaian households and businesses. The government has outlined four primary strategies to achieve debt sustainability:

1. Issuing additional debt to cover existing principal and interest payments,
2. Restructuring current debt,
3. Pursuing fiscal consolidation through budget adjustments, and
4. Monetizing the debt by issuing more cedis to inflate away the debt.

Since losing access to international markets in late 2021, Ghana has primarily relied on domestic borrowing, especially through treasury bills, alongside concessional loans from the IMF and the World Bank. In 2023, approximately GHS 48 billion was raised through the money market, covering 65% of the government's financing needs. This trend of relying heavily on treasury bills is expected to continue. Given the strong domestic demand for treasury bills and their exemption from the Domestic Debt Exchange Programme (DDEP), it's believed that the government will successfully secure the needed funds from the treasury bills market until it resumes bond issuance, anticipated in 2025. The government aims to issue a domestic medium-term bond in 2025 and regain access to the Eurobond market by 2027.

Another crucial step towards sustainable public debt is the restructuring of both domestic and external debts. The domestic restructuring has been largely successful, encompassing a wide array of debts except for treasury bills including ESLA, Daakye and USD denominated debt as well as Cocoa Bills issued by the Ghana Cocoa Board and non-marketable debt held by the Bank of Ghana. This move is projected to yield about USD 8 billion in debt relief from 2023 to 2026. Progress has also been made in external debt restructuring, with an anticipated USD 10.5 billion in debt relief over the same period, significantly aiding the path to sustainability.

Fiscal consolidation, the third strategy pursued by fiscal authorities to achieve the result illustrated in Fig 2, encompasses two main approaches: reducing government spending and increasing government revenue. The 2024 budget, as summarized in Table 3, outlines a plan to initially increase government expenditure from 21.5% of GDP in 2023 to 22% in 2026, before reducing it to 20.5%. In contrast, efforts to boost fiscal consolidation from the revenue side are expected to raise revenue from 15.8% of GDP to 18.2%. This indicates a predominant focus on enhancing revenue rather than balancing efforts between cutting expenditures and raising revenues. The government's heavy reliance on increasing revenue is evident through several revenue mobilization initiatives, including, among others, the introduction of a tax on Gross Gaming Revenue (GRR) to replace corporate income tax and VAT on betting and gaming. Another addition worth noting is the introduction of a withholding tax on winnings from betting and other games of chance. Also the budget re-introduces the minimum chargeable income receipt. There is also a new environmental excise duty and a 15% standard VAT rate on all commercial properties. We believe that while the fiscal consolidation measures are practical, they overly depend on increasing revenue. A more balanced approach, incorporating significant reductions in government spending, could enhance the effectiveness of these measures.

Table 3: Fiscal Consolidation Efforts

	2023	2024	2025	2026	2027
Expenditure (percent of GDP)	21.5	21.6	21.2	22	20.5
Revenue (percent of GDP)	15.8	16.8	17.3	18.2	18.2
Overall Balance (percent of GDP)	-5.7	-4.8	-3.9	-3.8	-2.3

Source: Ministry of Finance

The government's most significant strategy to steer public debt back to a sustainable path involves monetizing the debt through the Bank of Ghana (BoG), effectively reducing the real value of debt by inducing inflation. After losing access to international markets in late 2021, the BoG emerged as the principal financier of the fiscal deficit in 2022 and 2023, covering 38.5% and 37.1% of the deficit, respectively, and supporting the budget with a total of GHS 97.8 billion cedis. In the domestic debt restructuring process, the BoG's non-marketable holdings were reduced by 50%, and its marketable securities were exchanged on similar terms as those applied to other financial institutions, resulting in a total loss of GHS 55.12 billion for the central bank in 2022.

Although restructuring the BoG's debt holdings was crucial for achieving debt sustainability, the pivotal role played by inflation in this process cannot be overstated. According to Table 1, public debt as a percentage of GDP was 93.3% at the end of 2022 but was projected to decrease to 69% by the end of 2023. This significant reduction is attributed to an expected surge in GDP from GHS 610.2 billion in 2022 to GHS 850.6 billion in 2023, marking a 39.4% increase. While such GDP growth would typically be celebrated, in Ghana's case, the real GDP growth stands at only 2.3%, with the remainder being the result of the growth rate of the GDP deflator. Consequently, inflation (measured as the growth rate of the GDP deflator) is anticipated to decrease the public debt-to-GDP ratio by 22.9 percentage points, underscoring the central bank's critical contribution to restoring debt sustainability. The impact of inflation on lowering the debt-to-GDP ratio is anticipated to persist into 2024, a year in which the nominal GDP is projected to surpass the GHS 1 trillion mark and is expected to continue into the foreseeable future. However, this approach is expected to impose significant costs on Ghanaian households and businesses due to the adverse effects of inflation.

Among the four strategies deployed to restore public debt sustainability, monetizing the debt has been the most effective but also the most harmful to households and businesses, particularly affecting low-income groups due to the disproportionate impact of inflation. In contrast, fiscal consolidation, which has the least negative impact, has contributed the least to achieving debt sustainability.

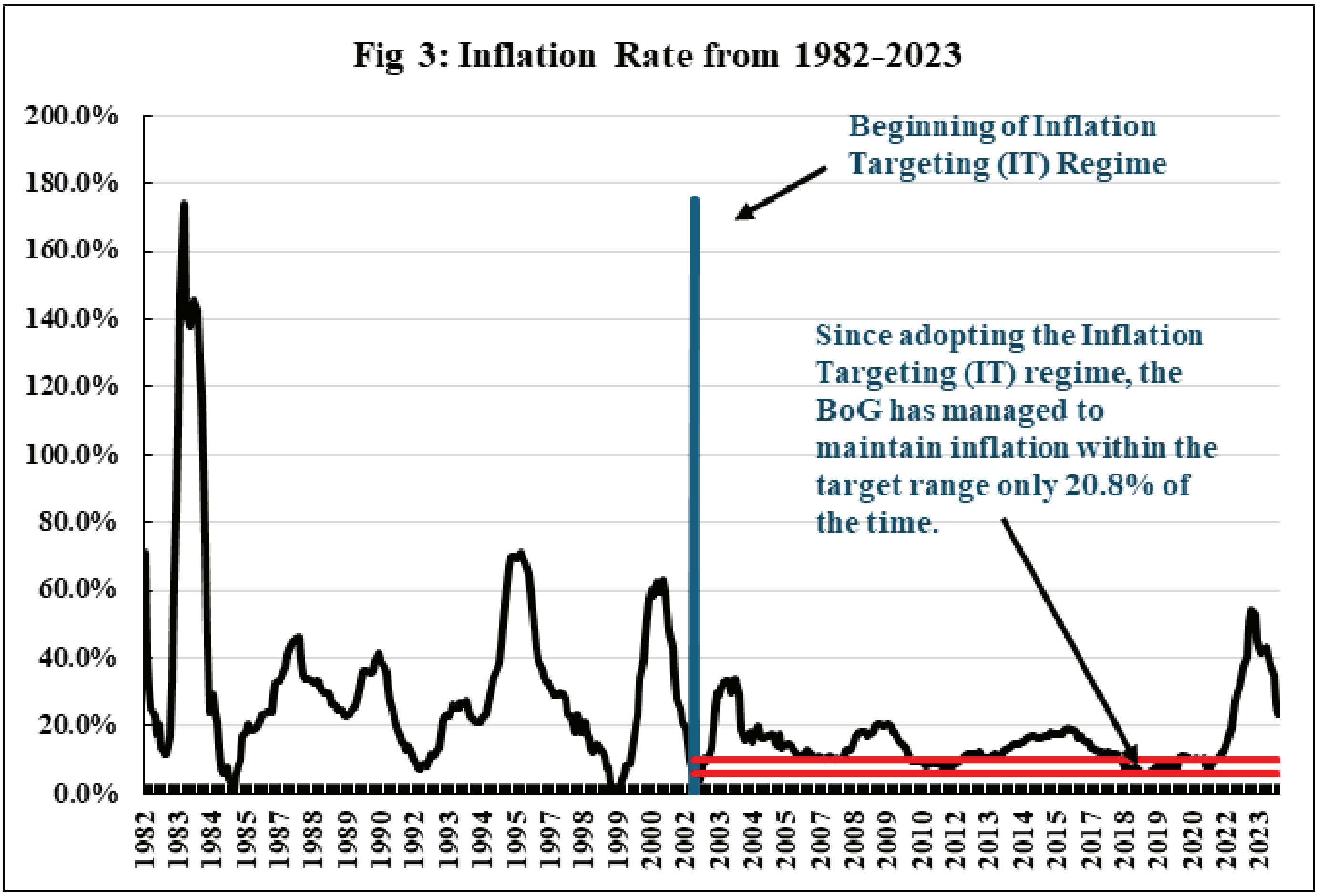
In summary, while the Minister of Finance aptly named the 2024 budget "NKUNIM," meaning victory, as it outlines a path to overcoming Ghana's pressing debt sustainability challenge, the victory seems confined to fiscal recovery. The strategies employed, notably the significant reliance on inflation, may lead to adverse outcomes for the average Ghanaian, especially those with lower incomes. While fiscal authorities may have navigated through the crisis, the broader population may still face hardships before conditions improve. Thus, although it marks a fiscal turning point, the victory may not be fully shared across all segments of the Ghanaian population.

PRICE STABILITY: REVISITING THE MANDATE OF THE BANK OF GHANA

The previous discussion outlined the pivotal role of the Bank of Ghana (BoG) in steering public debt towards sustainable trajectories. While fiscal authorities greatly benefit from debt sustainability, it's crucial to recognize that the Central Bank's measure of success is intrinsically linked to its mandate of price stability, not debt metrics. Price stability is essential for macroeconomic stability, and it is the bedrock for the Ghanaian economy. Getting inflation low and stable is crucial for the long-term economic wellbeing of every Ghanaian. Price stability is the responsibility of the Bank of Ghana. As stated under section 3 of the Bank of Ghana Act 2022 (Act 612), the primary objective of the Bank of Ghana is to maintain stability in the general level of prices. The Bank of Ghana officially adopted an Inflation Targeting (IT) framework in May 2002. The framework is designed to ensure price stability over the medium-term. At the institutional level, the Government and the Central Bank jointly set the medium-term inflation target, and the Bank of Ghana is required to deploy its policy tools to attain the target. Currently, the Bank's CPI inflation target is 8% with a symmetric band of 2%.

Evaluating the BoG's performance against its mandate prompts critical questions: After two decades, should there be a review of the BoG's price stability mandate, particularly its IT framework? This section endeavors to scrutinize the BoG's track record and proffer insights for enhancing price stability in Ghana.

As part of our forthcoming research agenda, we aim to conduct a comprehensive analysis of the economic repercussions stemming from the recent inflationary trends observed in Ghana. This investigation will meticulously evaluate both the advantages and disadvantages experienced by diverse economic stakeholders within the country. From a preliminary standpoint, the benefits of this inflationary period appear to be unequivocally positive for fiscal authorities. Specifically, the inflation has facilitated the possibility for fiscal authorities to steer public debt towards a more sustainable trajectory. However, the implications for households and businesses are far less clear at this juncture and, arguably, could be significantly adverse. Thus, the central question our research will seek to answer is whether the benefits realized by fiscal authorities in terms of debt sustainability outweigh the economic costs imposed on households and businesses.



Sources: Bank of Ghana, IMF

Fig 3 shows the Ghana's inflation trajectory from 1982 to 2023. Post-IT adoption, we witness a general moderation in inflation rates and reduced volatility. The pre-IT era (20 years preceding May 2002) had an average inflation rate of 37.7%, with a standard deviation of 28.7%, a stark contrast to the post-IT average of 15% and a standard deviation of 9.06%. While Fig 3 alone doesn't establish causality, the notable correlation between IT adoption and a more stable inflationary environment cannot be dismissed. However, the BoG's efficacy in adhering to its mandate could be considered lackluster. In the 260 months spanning May 2002 to December 2023, the BoG maintained inflation within the target rate in only 54 instances—accounting for a mere 20.8% of the time under the IT regime.

In Ghana, there's no legal requirement to regularly review the Central Bank's mandate. Yet, after 20 years of IT with only moderate success, it's clear that a thorough review is needed. We urge the next government to take a close look at the Bank of Ghana's (BoG) mandate. This review is particularly important given the observations of the current Vice President (Former Deputy Governor of BoG), Dr. Mahamudu Bawumia. In his book "Monetary Policy and Financial Sector Reform in Africa: Ghana's Experience," he discusses Ghana's shift from focusing on monetary aggregates to adopting an IT framework due to the former's frequent failure to meet its target. According to the book “the NPP government switched from the Monetary targeting regime to inflation targeting regime because monetary targeting had not yielded the desired results judging from its frequent divergence of actual monetary growth from targeted monetary growth.”

Despite BoG's proactive measures, from pioneering digital currency initiatives to contributing to debt sustainability, achieving its core mandate of price stability remains a challenge. This reality calls for a thorough review of BoG’s mandate.

ELECTION OUTCOMES AND ECONOMIC PERFORMANCE

As we approach the 2024 elections, it is timely to address the prevailing discourse regarding the economic implications of governance by the two predominant political parties in our nation, the New Patriotic Party (NPP) and the National Democratic Congress (NDC). Common sentiment often suggests that the economic performance of the country is contingent upon which of these parties is at the helm.

To objectively evaluate this claim, we have analyzed data spanning from 1992 to 2023, encompassing five critical macroeconomic indicators: real GDP growth rate, real GDP per capita growth rate, average inflation rate, public debt-to-GDP ratio, and the rate of depreciation of the Ghanaian cedi.

Fig 4 shows the performance the key macroeconomic variables under the stewardship of both the NPP and NDC. Our analysis reveals a nuanced picture. Contrary to popular assertions, the empirical evidence does not robustly support the notion that economic performance is superior under either party's regime. Specifically, for four of the indicators — real GDP growth rate, per capita growth rate, average inflation, and public debt-to-GDP ratio — our findings indicate no statistically significant divergence in performance between the administrations of the NPP and NDC. However, a notable exception lies in the currency domain. Our findings indicate a statistically significant trend concerning the cedi's depreciation rate: under NPP-led governments, the cedi has demonstrated greater resilience, depreciating at a lower average rate of 10.4%, which stands in stark contrast to the higher depreciation rate of 19.9% observed during NDC administrations.

In summary, while political leadership can indeed influence economic policy and outcomes, our analysis suggests that, with the exception of currency depreciation, there is limited evidence to conclusively declare one party as the superior economic steward over the other.

PERFORMANCE OF MACROECONOMIC VARIABLES NPP VS NDC

Key Macroeconomic Variables	Average Values		Verdict
	NPP-led	NDC-led	
Real GDP Growth Rate(%)	5.1	5.4	Not Statistically Significant
Per Capita Growth Rate(%)	2.6	2.5	Not Statistically Significant
Average Inflation Rate(%)	17.6	20.1	Not Statistically Significant
Public Debt-to-GDP ratio (%)	53.6	45.2	Not Statistically Significant
Cedi Depreciation(%)	10.4	19.9	Statistically Significant

- **MY ANALYSIS FINDS INSUFFICIENT EVIDENCE TO CLAIM SUPERIOR ECONOMIC PERFORMANCE UNDER EITHER THE NPP-LED OR NDC-LED ADMINISTRATIONS.**

Fig 4: Performance of Key Macroeconomic Variables NPP vs NDC