



# Cutting Rates While Draining Liquidity: Is the Bank of Ghana Contradicting Itself—or Getting It Right?

**W**hen a central bank cuts interest rates while simultaneously spending billions to withdraw liquidity from the system, it is reasonable to ask: are these policies pulling in opposite directions?

This question arises from a deeper curiosity about how monetary policy is currently being conducted in Ghana. Over the past several months, the Bank of Ghana has been engaged in what appears to be a deliberate pattern: **gradually reducing the policy rate while at the same time intensifying efforts to withdraw excess liquidity from the financial system.** The most recent decision to lower the policy rate from 15.5 percent to 14 percent simply brings this pattern into sharper focus. It is not an isolated move, but part of an ongoing cycle of easing interest rates alongside continued sterilization. At the same time, the scale of liquidity management has been substantial. The Governor recently disclosed that the Bank incurred about GH¢17 billion in 2025 in absorbing excess liquidity from the system.

At first glance, the combination seems puzzling. Lower interest rates are often associated with injecting liquidity. Sterilization removes liquidity—at a cost. Why do both at once?

The answer lies in recognizing that monetary policy operates through multiple channels, each targeting a different objective.

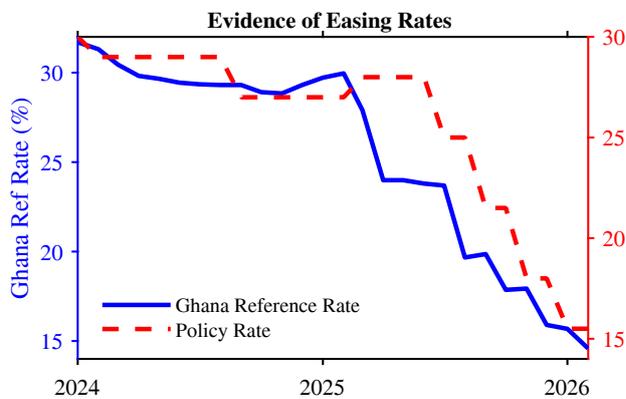
## The Evidence: Easing Rates, Tightening Liquidity

The data presents a clear and consistent picture. On one hand, interest rates across the economy have declined sharply. The interbank rate has fallen from above 27 percent in early 2025 to about 12.6 percent by February 2026, closely tracking the downward path of the policy rate (As shown in Figure 1). Treasury bill yields and lending rates have followed a similar trend. The sharp decline in the Ghana Reference Rate—from 32.17 percent in January

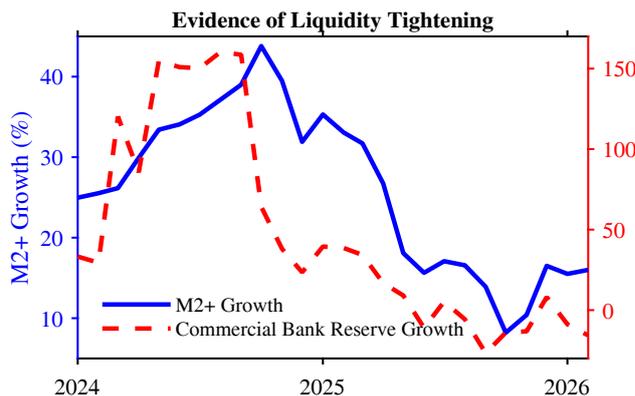
2024 to about 11.7 percent—further confirms that these policy rate reductions have been transmitted effectively into domestic financial conditions. This provides strong evidence that monetary easing is taking place through the interest rate channel, lowering the cost of credit across the economy.

At the same time, liquidity indicators tell a different but equally important story. As illustrated in Figure 2, system-wide liquidity has been tightening. Commercial banks’ reserves held at the Bank of Ghana—a key measure of available liquidity—have declined significantly, from over 74 billion cedis earlier in 2025 to about 60.8 billion cedis by February 2026. Moreover, the growth rate of these reserves has been predominantly negative since mid-2025, indicating sustained liquidity absorption. This pattern is reinforced by broader monetary aggregates. Growth in total liquidity (M2+) has moderated markedly, averaging below 20 percent over the past year, a clear slowdown from earlier expansion.

### Monetary Rate Easing and Liquidity Tightening in Ghana



**Figure 1: Evidence of Easing Through Interest Rates:** The figure shows that since January 2024, the Bank of Ghana has reduced the policy rate by a cumulative 15.5 percentage points. This easing has transmitted clearly into domestic financial conditions. In particular, the Ghana Reference Rate (a key benchmark for pricing loans) has declined sharply from 32.17 percent in January 2024 to about 11.7 percent currently. The Ghana Reference Rate reflects broader monetary conditions, as it is determined by a weighted average of the 91-day Treasury bill rate, the Monetary Policy Rate, and the interbank overnight rate. Its sustained decline provides strong evidence that policy rate reductions have effectively lowered borrowing costs across the economy.



**Figure 2: Evidence of Tightening Liquidity:** The figure shows a marked slowdown in liquidity growth from early 2024 to the present. In particular, the growth rate of commercial banks reserves held at the Bank of Ghana has been predominantly negative since mid-2025, reflecting sustained and deliberate liquidity absorption by the central bank. This tightening is also evident in broader monetary aggregates. The growth of total liquidity (M2+) has moderated significantly, averaging below 20 percent over the past year, compared to much higher rates during the earlier expansion phase. Together, these trends provide clear evidence that, alongside easing interest rates, the Bank of Ghana has been actively withdrawing excess liquidity from the banking system.

Taken together, the evidence shows two developments occurring simultaneously:

- Interest rates are falling, easing financial conditions
- Liquidity is being withdrawn, tightening system-wide cash balances

## Two Channels, Two Objectives

These developments are not contradictory. They reflect monetary policy operating through two distinct channels at the same time.

## The Interest Rate Channel: Supporting Domestic Recovery

The policy rate governs the cost of borrowing. With inflation now down to about 3.3 percent, the need for very high interest rates has diminished. Keeping rates elevated would unnecessarily constrain credit, investment, and growth. The recent rate cut is therefore aimed at:

- easing financing conditions
- supporting private sector activity
- sustaining economic recovery

## The Liquidity and Exchange Rate Channel: Preserving Stability

At the same time, the Bank is managing a large overhang of excess liquidity in the system accumulated during the crisis period of 2022–2023. In Ghana’s context, this is critical because liquidity and exchange rate dynamics are closely linked. Excess cedi liquidity does not remain idle. It often flows into the foreign exchange market, increasing demand for dollars and putting pressure on the exchange rate. Exchange rate instability, in turn, feeds back into inflation. Sterilization operations address this risk by:

- absorbing surplus reserves
- limiting speculative demand for foreign exchange
- strengthening the stability of the cedi

## Why Not Do Neither?

This is the most important question. If lowering rates is associated with liquidity injection and sterilization withdraws liquidity, why not do neither—and avoid the cost altogether? This is because the two actions are not substitutes. They do not cancel out. They operate on different margins of the economy.

- The policy rate determines the price of short-term funds
- Sterilization determines how liquidity is allocated and used, especially in sensitive markets like foreign exchange

The liquidity associated with a rate cut is typically targeted and limited, aimed at guiding short-term interest rates downward. The liquidity being withdrawn, however, is structural and much larger, accumulated during the crisis period. If the Bank were to do neither:

- Borrowing costs would remain unnecessarily high
- Excess liquidity would continue to circulate
- Exchange rate pressures could re-emerge
- Monetary policy transmission would remain weak

In effect, the economy would face tight credit conditions alongside renewed financial instability.

## A Lesson from the United States

A useful comparison comes from the United States, where recent monetary policy provides a clear example of how these dynamics can coexist. Over the past year, as inflation eased, the U.S. Federal Reserve began cutting its policy rate. Starting in September 2024, when the policy rate stood at 5.25 percent, the Fed reduced rates by a cumulative 175 basis points to about 3.5 percent by December 2025. At the same time, however, the Fed continued its program of quantitative tightening (QT)—systematically reducing its holdings of government securities and other assets. This led to a decline in the Fed’s balance sheet from approximately US\$7.1 trillion to US\$6.5 trillion, representing about an 8 percent contraction. This reduction is particularly striking when viewed against the earlier expansion: the Fed’s balance sheet had surged from about US\$4.2 trillion in February 2020 to US\$8.9 trillion by June 2022 in response to the COVID-19 crisis.

The data therefore shows two movements occurring simultaneously:

1. policy rates declining, and
2. central bank assets shrinking.

This was not interpreted as a contradiction. Rather, it reflected two distinct policy tools operating in parallel:

1. Rate cuts to ease short-term borrowing conditions
2. Quantitative tightening to withdraw excess liquidity accumulated during earlier stimulus

In essence, the Fed was lowering the price of money while normalizing the quantity of liquidity. The Bank of Ghana is now operating under a similar logic—adapted to Ghana’s own economic realities.

## A Deliberate Policy Mix

What may appear contradictory is, in fact, careful policy calibration.

The Bank of Ghana is:

- lowering interest rates to support recovery
- withdrawing excess liquidity to protect the exchange rate
- reinforcing macroeconomic stability

This is not inconsistency. It is coordination.

## Conclusion: Not a Contradiction, but a Balancing Act

The Bank of Ghana is not working at cross purposes. It is navigating a complex transition—from stabilization to recovery—using more than one instrument at a time. Lowering the policy rate supports growth by easing the cost of credit. Withdrawing excess liquidity safeguards stability by limiting pressures on the exchange rate. These actions may move in opposite directions on the surface, but they are aligned at a deeper level: both are aimed at sustaining macroeconomic stability while supporting a gradual recovery. The real challenge for

monetary policy today is not choosing between easing and tightening. It is knowing where to ease, where to restrain, and how to do both without undermining either objective. And in that respect, the Bank of Ghana's current approach is not a contradiction—it is a balancing act.

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