

MPC Cracks the Whip on Low Lending with The Recalibrated CRR Directive; Could Stimulate Nearly GHS50 Bn in New Lending to Support Growth

The Monetary Policy Committee, while maintaining the policy rate at 29% at its 117th policy meeting earlier last week, also recalibrated the Cash Reserve Ratio (CRR) based on the Loan-Deposit (L/D) ratio. This action is a departure from the unified CRR that prevailed previously and, perhaps, was the main plot of the 117th MPC meeting. Per the new CRR directive, banks with an L/D ratio above 55% will continue to maintain CRR at the current rate of 15%. However, effective April 1, 2024, universal banks with L/D ratio between 40% to 55% and less than 40% are required to maintain a Cash Reserve Ratio of 20% and 25%, respectively, an increase of 5% and 10% for the two categories from the current level.

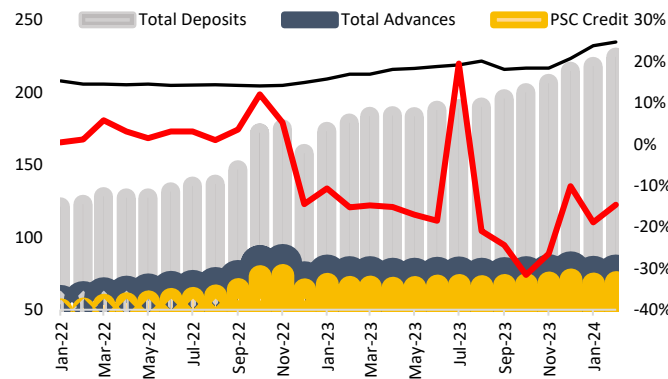
With this directive, we believe the MPC aims to stimulate loan book expansion to support real sector growth, particularly given the austerity regime, which limits fiscal and monetary policy support for the below-trend growth. The BoG may also be limiting the cost of its Open Market Operations (OMO) with this new CRR directive while supporting its inflation objectives amidst the highly liquid interbank market conditions. In this note, we assessed the directive's implications for commercial banks, deficit financing, real sector credit, growth prospects, and the Bank of Ghana.

Background – Increased risk aversion amidst the uncertain operating environment and deteriorating asset quality undermined credit growth: The post-DDEP market has been characterized by robust deposit growth, with the updated banking sector data showing a 25.5% y/y growth in deposits in Feb-2024 to GHS224.4 bn (+GHS45.6 billion). However, total loans and advances have been sluggish, growing by a paltry 1.77% y/y to GHS74.8 billion (+GHS1.3 billion). In Nominal terms, private sector credit grew by 5% (+GHS3.3 bn) to GHS68.8 bn but contracted by 14.7% to GHS 331.1 mn in real terms. Thus, the cash-rich banks have adopted a conservative credit stance, favouring the high-yielding T-bill and OMO Bill investments to credit creation as a strategy to preserve capital amidst declining asset quality in an uncertain operating environment. Within the 1-year period post DDEP, banks have grown their investment portfolio with a chunk of their deposits, increasing their holding of T-bills and OMO Bills by 67.6% y/y (+GHS53.6 bn) at the close of Feb-24.

Given the need to anchor the disinflation process firmly, the Bank of Ghana has had to mop up the excess liquidity through its OMO operation at a significantly high cost. Again, the limited fiscal and monetary support for economic activity and the tight credit stance have kept growth sluggish and below trend despite closing 2023 ahead of the IMF programme assumptions. Thus, by this new CRR directive, the MPC may be attempting to stimulate loan book expansion to drive growth in the real sector while keeping the inflation objective on track.

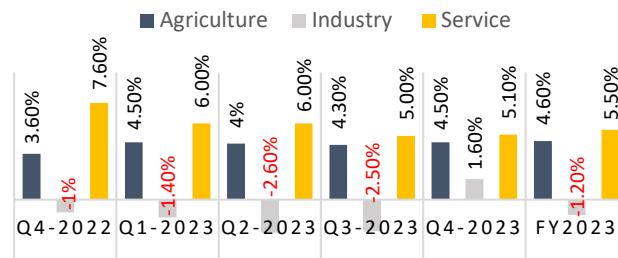
The Banker's Dilemma - Advance GHS47Bn in new loans or keep an extra GHS17.9bn in reserves with BoG at no interest. With this directive kicking in from April 1, our analysis of the 9 Months and FY-23 numbers for 22 out of the 2023 banks (excluding NIB) show that, without any immediate reaction, these 21 banks must deposit an additional GHS17.9 bn with the Bank of Ghana in complying with the new directive. Of the 22 banks, only SOGEGH has an L/D ratio above 55% (74.61% as of Sept-2023) and will maintain a CRR of 15%. Six banks – ADB, BOA, FNB, CAL, RBGH and PBL- have L/D ratios between 40% and 55%, falling in the 20% category. Together, these six banks must advance about GHS3 bn in new loans to move into the 15% CRR category or deposit an additional GHS1.44 billion with the Bank of Ghana to keep up with the 20% CRR directive. The remaining 15 banks, dominated by the top 10 banks (by total assets), have L/D ratios ranging between 15.5% and 39%) and, thus, fall in the 25%

Figure 1: Growth in deposits, loan and advances and private sector credit



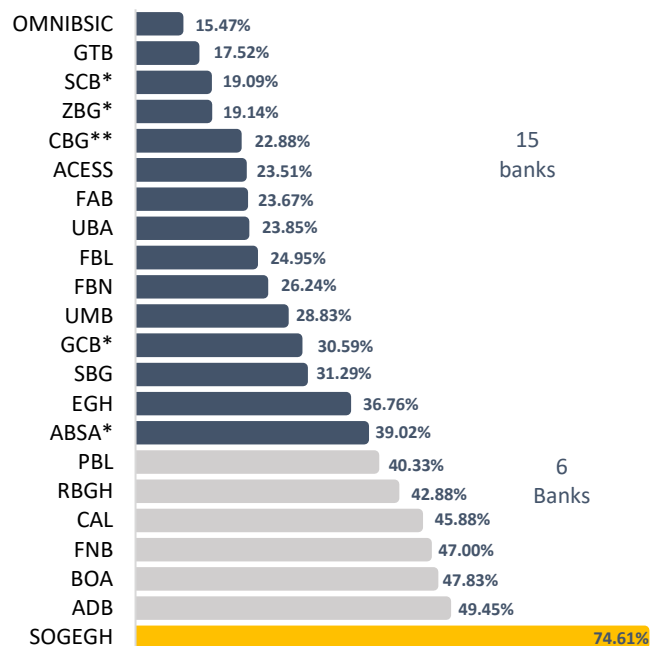
Source: GCB Capital Research | Bank of Ghana

Figure 2: Quarterly GDP Growth By Sector



GCB Capital Research | Ghana Statistical Service

Figure 3: L/D Ratio using end-Q3 and FY-23 numbers



FY-2023 - * | 1Q23 - **

category. Together, this tier of 15 banks will have to increase their loan portfolio by GHS 19.7 bn to move into the 20% CRR category and by a further GHS26.4 billion to move from the 20% bracket to the 15% bracket. Thus, using the latest available numbers, the 22 banks will be required to grow their loan portfolio by about GHS49 Bn to avoid keeping an additional GHS17.9bn with the Bank of Ghana in keeping with the new directive.

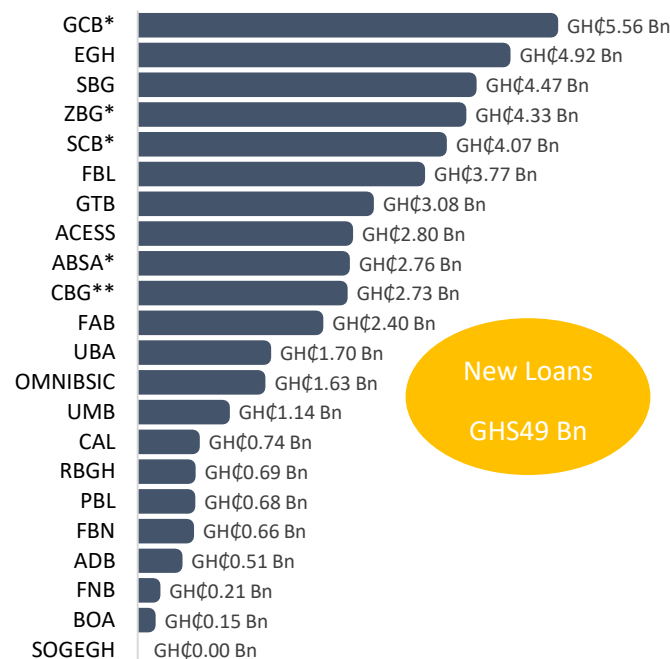
Given the uncertain operating environment and the rising NPL levels, this is a tough task, potentially signaling the end of an era of "free cash" for banks from passive investment in attractively priced money market instruments, particularly as the strong rebound in profitability in 2023 was mainly driven by investments. Banks may now earn profit "the hard way" through credit creation. While an additional deposit of GHS17.9 bn at zero interest will reduce earnings and increase the cost of deposits, we believe the credit stance will remain cautious, given the deteriorating asset quality. We expect loan book expansion to be gradual, particularly as banks try to preserve capital, restore capital adequacy, and wean themselves off regulatory forbearance.

MOF will have to re-think deficit financing, and yield compression could buck the trend as Banks focus on new ways to deploy deposits: Commercial banks hold the largest share of T-bills, accounting for over 35% of the outstanding stock of T-bills in Feb-24. While all banks hold healthy cash balances on their books, we believe these are largely optimal cash balances required for smooth operations. Consequently, we expect the banks to gradually liquidate parts of their T-bill holdings to fund credit creation, which will significantly reduce demand for T-bill going forward, as we have already seen in the 43% undersubscription at Auction 1896, the first time in 17 actions. From our estimation, the weekly T-Bill maturity obligations will average GHS3.5 bn in 2Q-2024 (vs GHS3.2bn in Q1 2024). With the T-bill currently a dominant domestic source of funding for the budget, reduced demand from banks increases the risk of uncovered auctions and poses an upside risk to the cost of short-term borrowing. Thus, the pronounced under-subscription at the last T-bill auction could persist beyond the current week, with the pace of yield compression potentially softening or may even buck the trend through Q2 2024, all things equal.

Timely support for private sector credit growth with the anticipated competition for quality borrowers potentially driving lending rates lower: We expect the competition to lend to the blue-chip corporates to gradually heat up through 2Q 2024 as banks carefully expand their loan book to enjoy the base CRR bracket. With the growth outlook still subdued relative to the trend, increased lending will be a timely boost for activity and new investments in the private sector. Key players across the agriculture, industry and services sectors could thus position themselves to tap into this anticipated credit growth. The competition will likely lower lending rates marginally from the average of 32.8% in Feb-2024 once the macroeconomic fundamentals continue improving.

The BoG sustains efforts to rein inflation while managing the cost of its OMO operations: The BoG continues using the CRR and the monetary policy rate as key policy tools to steer inflation on the lower path. The latest CRR directive adds to the net increase of 2% in the CRR in 2023, helping the BoG to mop up excess liquidity from the banking sector at no cost. We expect the liquidity squeeze from this directive and the continuously tight monetary policy stance to anchor the disinflationary process against the simmering price pressures in the near term. Consequently, we do not envisage any policy rate action at the May 2024 policy meeting as the anticipated increase in inflation for March 2024 will be transitory, and the disinflation process could resume from Apr-2024.

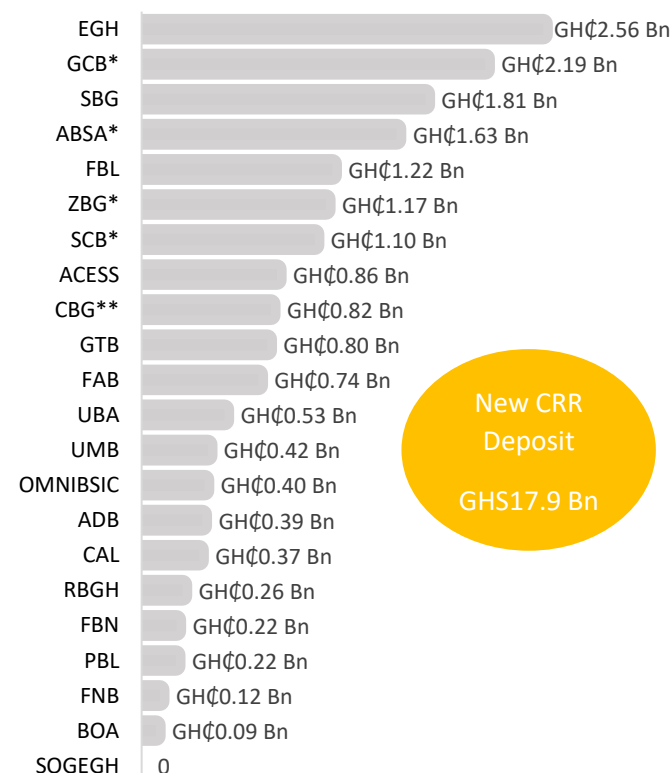
Figure 4: The road to 15% – New loan required for the 15% CRR Bracket.



Source: GCB Capital Research | Ministry of Finance

GCB Capital Research | Bank of Ghana

Figure 5: Additional deposit required to comply with the new CRR Directive



Research Contacts

Courage Kwesi Boti

Economist/ Research Lead

+233302945848 | +233302945838

ckboti@gcb.com.gh

Fund Management Contacts

Afua Akyaa Osei

Vice President, Fund Management

+233302945848 | +233302945838

aaosei@gcb.com.gh

Wilson Kyeremeh

Portfolio Manager, HSG

+233302945848 | +233302945838

wkyeremeh@gcb.com.gh

Advisory & Capital Markets Contacts

Michelle Nana Ohenewaa Kitson-Amoah

Associate, Advisory & Capital Markets

+233302945848 | +233302945838

mnodadey@gcb.com.gh

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49 Ndabaningi Sithole Rd

Labone, Accra