Economic and Market Insight

Policy Update: March 2024 Monetary Policy Update

March 2024

GCB CAPITAL LTD

Research & Analytics

MPC Holds Policy at 29% in Mar-24 but Altered the CRR Significantly Ostensibly to Drive Credit Growth

Summary

- *No Surprises as the MPC keeps the policy rate at 29% amidst emerging upside risks to inflation.*
- *MPC cracks the whip on low lending with the recalibrated CRR directive, potentially signalling the end of 'free money' for banks*
- *Debt standstill and reduced portfolio reversals yield C/A and overall BoP surplus in 2023, which partly underscores Cedi's resilience relative to 2022 and 2023.*

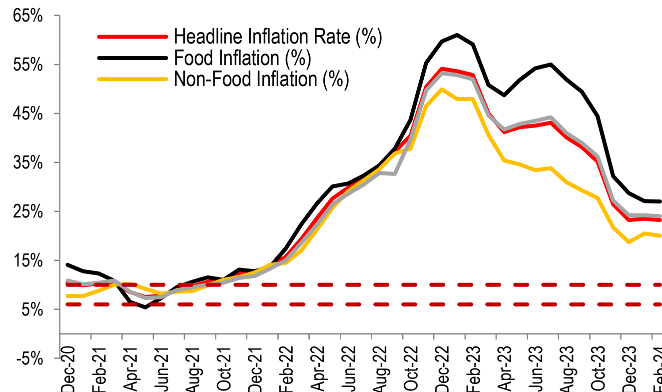
MPC stays rate at 29%, recalibrates CRR to encourage loan book expansion: After pivoting in Jan-24, the Monetary Policy Committee (MPC) kept the Monetary Policy Rate at 29% amidst a slightly elevated inflation profile. According to the MPC, possible upward revisions in transport fares, adjustments in utility tariffs, higher ex-pump prices, and some pass-through effects of exchange rate depreciation have slightly tilted the risks to inflation on the upside and require close monitoring. Additionally, the MPC recalibrated banks' Cash Reserve Ratio (CRR) requirements, potentially to stimulate credit growth, particularly in the private sector. Effective April 2024, banks with a Loan-Deposit (L/D) ratio between 40% to 55% and less than 40% are required to maintain a Cash Reserve Ratio of 20% and 25%, respectively, with the Bank of Ghana. However, the CRR is maintained at 15% for banks with L/D greater than 55%.

No surprises as the upside risks to inflation simmer: The decision aligns with our expectations and the consensus market forecast. While there was scope for a marginal rate cut, the current and emerging upside risks to the inflation outlook and expectations require a cautious policy stance. Despite the local unit's relatively stable run (compared to 2022 and 2023), the elevated corporate FX demand from late Feb-24 kept the local unit under pressure. Thus, the Cedi has shaved off 7.52% YTD against the USD and is equally weak against other major trading currencies across the interbank and retail markets. We also see the continuing uptick in crude oil prices largely from supply shocks due to Geopolitics and the Red Sea attacks on cargoes, resulting in increases in fuel prices. In response, the major oil marketing companies have thus far increased the prices of gasoline and gas oil by 8.88% and 11.55%, respectively, at the pumps, which may trigger potential increases in transport fares and general prices. Thus, the anticipated pass-through of the currency pressure to inflation and the inflationary effects of the rising fuel costs and their combined implications for the quarterly utility tariff review pose upside risks to inflation in the near term. We expect inflation for Mar-2024 to print significantly higher (GCL outlook for Mar-24 inflation: 26%) due to these risk factors and unfavourable base effects before resuming a decline from Apr 2024. Therefore, we believe the rate-neutral decision is appropriate for signalling a continuously tight monetary policy stance that is required to anchor the disinflation process firmly.

Insights from the Summary of Economic and Financial Data

MPC cracks the whip on low lending with the recalibrated CRR directive: While total deposits of the banking sector grew by 25.5% y/y in Feb 2024 to GHS224.4 bn (+GHS45.6 bn), loans and advances grew by a paltry 1.77% y/y to GHS74.8 bn (+GHS1.3 bn). Private sector credit increased by 5% to GHS68.8 bn (+GHS3.3 bn) but contracted by 14.7% to GHS 331.1 million in real terms. The data shows that banks have generally channelled their deposits into investment (in GoG Bills and BoG OMO Bills), with the investment portfolio increasing by 67.6% y/y (+GHS53.6 bn) amidst the increased aversion to loan book expansion due to the uncertain operating environment. Thus, we see the CRR recalibration as an intervention to stimulate loan book expansion and drive growth in the real sector amidst the limited policy support for growth.

Figure 1: *Year-on-year Headline Inflation Dynamics*



Source: GCB Capital Research | Central Bank Websites | Ghana Statistical Service

Figure 2: ***The Trajectory of Inflation and the Monetary Policy Gap***

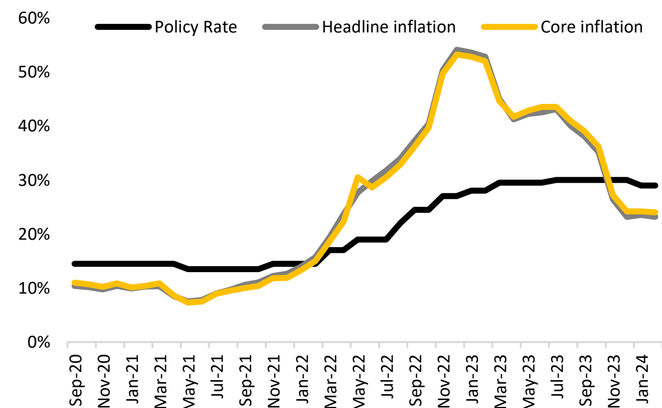


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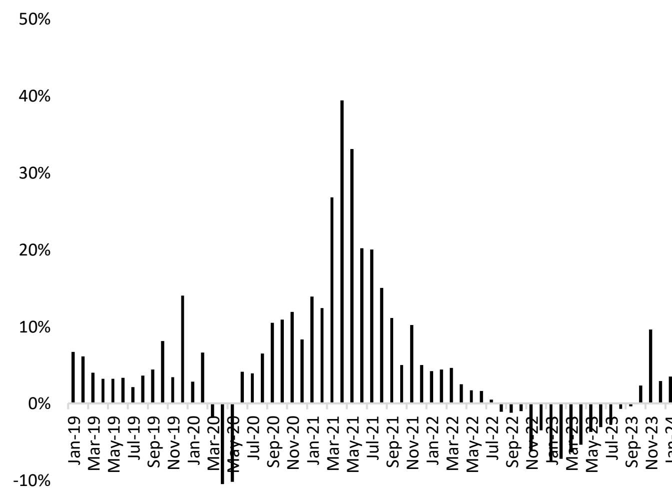
Figure 3: ***Trajectory of economic activity depicted by the Composite Index of Economic Activity (CIEA)***



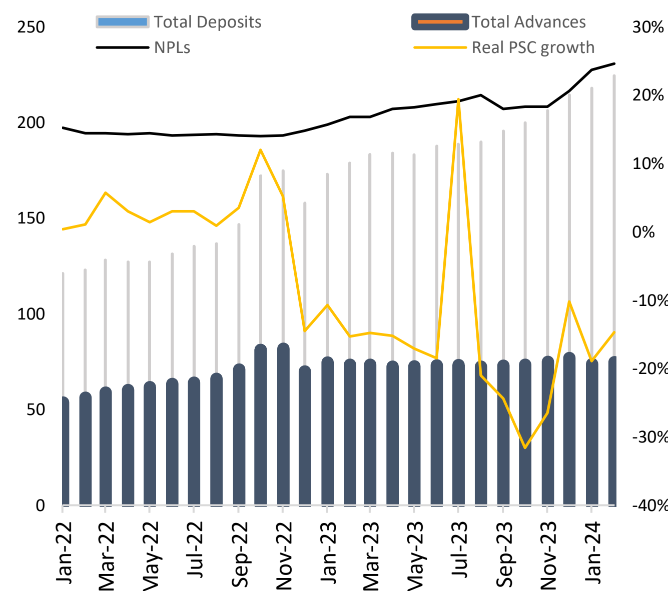
Analyzing the latest available financial data of the banks (9 Months 2023), only GT Bank (with L/D of 74.82%) will maintain a CRR at the current 15%. About six banks, mostly mid-tier and lower-tier banks, fall within the 40% to 55% L/D category and will be required to maintain a CRR of 20%. The remaining 16 banks, dominated by the top ten (10) banks, have L/Ds between 15.5% and 25% and will be required to maintain a CRR of 25%.

No more 'free money' following the CRR Directive with the Treasury also potentially facing a higher cost of funding: It appears the era of 'free cash' from passive investments driving profits is over as banks will now have to 'earn' their profits. As a result, we expect a drastic decline in banks' appetite for T-bills in favour of credit creation to avoid the higher brackets of the new CRR directive. Thus, we see the orientation gradually shifting towards a more aggressive credit stance, which will have ramifications for the government's deficit financing operations and the real sector. For the real sector, the competition for quality credit could drive down lending rates and, potentially, stimulate growth through increased investments. However, with banks dominating T-bill holding (banks held 35.3% of outstanding FV of T-bills as of Feb-24), the anticipated reduction in demand for T-bills could result in a higher interest cost for the Treasury's funding operations immediately. With the BoG also facing high-interest costs (around the policy rate) for its OMO operations amidst the need to mop up excess liquidity to douse inflation, the directive will sweep substantial liquidity from the system (without the bank's response) at no cost to the regulator.

The C/A closed 2023 in surplus thanks to the debt standstill: From a deficit position of US$1.52 billion in 2022, the current account recorded a surplus of US$1.11 bn in 2023 following reduced income and interest outflows due to the temporal external debt standstill that took effect from Dec-2022. The summary of economic and financial data showed that the balances on trade in goods and services had little change from 2022. However, net income payments declined sharply to US$2.08 bn (-60% y/y), with external debt service following the debt standstill also declining by 89.5% y/y to US$0.17 bn. Thus, this significantly reduced the net outflow position, and the 14% increase in inward remittances helped the current to close in the a surplus.

The surplus current account, together with the significantly reduced portfolio reversals, yielded an overall BoP surplus in 2023: While FDI inflows declined by 11.8% y/y, portfolio reversals slowed sharply in 2023 to a net outflow of US$274.5 mn (+86.7% y/y) following the Domestic Debt Exchange, which limited activity in the secondary bond market and the opportunities to externalize. Consequently, the capital account recorded a significantly lower deficit of US$756.2 mn (+ 64.7% y/y) relative to 2022, with the combined effects of the developments in the current and capital account yielding a surplus overall Balance of Payment (BoP) worth US$0.462 billion in 2023, which underscored the Cedi's relative stability vs the major trading currencies beyond Jan 2023 and through the seasonality pressures in Q1 2024. While the significant outlay on energy sector-related payments in Q1-2024, the strengthening USD and elevated corporate FX demand pressures have pinned the Cedi back from mid-February amidst delayed disbursement from the World Bank for budgetary support, the tight monetary policy stance and the imminent World Bank and Cocoa sector inflows could improve FX liquidity conditions. Reserve build-up also appears ahead of schedule, further supporting the near-term outlook. However, the growing import bill as economic activity recovers, lingering global uncertainties due to Geopolitics, and the still uncertain domestic operating environment pose some risks to the outlook in the near term. We see the Cedi continuing in the slightly bearish mode through 2024 but within a predictable band relative to 2022 and 2023.

Figure 4: ***Deposits, Advances and growth in private sector credit***



Source: GCB Capital Research | Ministry of Finance

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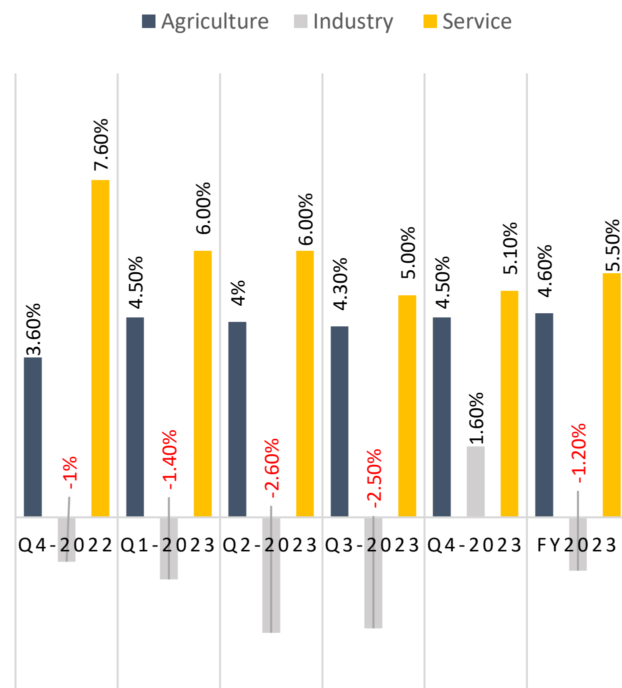
Figure 5: Quaterly GDP Growth Trend by Sector



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

3