Investor Update | Economy | MPC Update

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Databank
Leadership

The MPC Surprises the Financial Market with 200bps Cut in MPR for March 2017

The Monetary Policy Committee (MPC) of the BoG cut the Monetary Policy Rate (MPR) by 200bps to 23.5% at its second MPC meeting of 2017.The committee cited sustained decline in inflation and diminished underlying inflation pressures as factors underpinning the decision. While monetary policy easing was broadly expected, the magnitude of the cut (the highest since Feb-2010) was rather a pleasant surprise to the financial markets as the committee seeks to complement fiscal policy in stimulating economic growth in 2017.

Justification:

Given the implicit tightening in inflation since Oct-2016, Ghana is on course to meet its medium-term inflation target of 8±2% by 2018. The external sector continues to improve, the depreciation pressures observed for most part of Q1-2017 have subsided and government appear to be committed to fiscal consolidation. Economic growth however fell below target in 2016 and could remain below potential in 2017. The committee, notwithstanding the external headwinds to price and exchange rate stability, moved to ease the monetary policy rate to provide impetus for economic growth.

Our Broad Views on the Policy Stance:

- The monetary policy decision seeks to complement government's fiscal policy in stimulating Economic growth.
- The uncertainties about the direction of fiscal policy in 2017 and higher than targeted fiscal deficit delayed monetary easing despite the steady path of disinflation. This rate cut is therefore an accumulation of delayed monetary easing.
- The following domestic and external headwinds could threaten macroeconomic stability in Ghana in 2017:
  - Unstable commodity prices on the international markets could destabilise Ghana's Balance of Payment position and dampen the exchange rate outlook
  - Shortfalls in tax revenue mobilisation could undermine fiscal consolidation
  - Expected fiscal stimulus in the US and a recovery in the Eurozone could tighten the global financial markets and distort exchange rate stability, BoP and inflation outlook.

For more analytical discussion on African currencies, equities and fixed income investments, kindly contact:
Databank Research Team
research@databankgroup.com
Tel: +233 (0) 302 610 610 | Fax: +233 (0) 302 681443

To place orders for Ghana's T-Bill and T-bond securities as well as stock market investments, kindly contact:
Databank Brokerage Team
+233 (0) 302-610610 Ext. 1705
fixedincome@databankgroup.com
brokeragestaff@databankgroup.com

Developments in Key Macroeconomic Indicators

Indicator	FY-2016 (Provisional)	2017 Projections (GoG)	Provisional Outturn (2017)
Fiscal Deficit	8.7% (cash basis)	6.5%	-
End Period Inflation	15.4%	11.2%	Feb-2017: 13.2%
91-Day Yield	16.43%	3.12%	Mar-2017: 17.51%
USD/GHS Dep. Rate	9.65%	15.7%	3.46%
Gross Reserves (import cover)	(3.5 months)	≥3 months	Feb-2017: (3.7months)
Gross Reserves	$ 6.16 bn	-	$ 6.46 bn
Gross Public Debt (% of GDP)	Gh¢122.3 bn (72.5%)	- (70.9%)	-
Tax revenue-to-GDP Ratio	15.2%	16.9%	-
Expenditure/GDP	30.3%	28.6%	-
NPL Ratio	17.3%	-	Feb-2017: 17.7%

*Source: Databank Research, Bank of Ghana **Data as at Nov-2016*

Our Assessment of Latest Macroeconomic Data

The MPR Rate Cut Could Boost Credit Growth and Private Sector Investment: The economy is projected to grow by 6.3% in 2017 mainly underpinned by an expected increase in oil & gas production and increased private sector investment. Our examination of the summary economic and financial data revealed that private sector credit growth of 14.4% for FY-2016 was sluggish (FY-2015: +24.5%). This was mainly due to high NPL ratio resulting from SOE and energy sector debt while lending rates were extremely high, reinforcing the rising NPLs.

Following the restructuring of the energy sector debts however, the NPL ratio has improved slightly, declining from a peak of 19% in Oct-2016 to 17.7% in Feb-2017. Given that the current government is considered private sector oriented, the policy rate cut is expected to complement fiscal policy in stimulating increased private sector investment and increased productivity. We expect nominal interest rates on short-term treasury bills to decline broadly, helped in part by the government's deliberate effort to reduce its participation at the shorter end of debt market. As a result we expect a moderate growth in private sector credit.

Improving External Balance Could Supports Bullish Outlook for the Cedi in the Medium to Long Term: An improvement in Ghana's external balance is expect to support stability of the Cedi in the months ahead. Available data from the bank of Ghana suggest that market apprehension resulting from elevated fiscal risks was largely responsible for the sharp depreciation in the Cedi early in Q1-2017 (-8.8% by mid-March).

We observed that, trade balance has improved by nearly 200% y/y to $573 M (1.3% of GDP) as at Feb-2017 (same period last year: -$574.1 M). The surplus BoP position resulted from a 57% y/y growth in export revenue to $2.49 bn while import expenditure decline by 11% y/y to $1.91bn. As a result, Ghana's gross foreign reserve position has improved by $293.5 M to $6.45 bn (3.7 months of import cover) in the first two months of 2017.

We see this improved reserve position as largely resulting from BoP surplus, which may not sustainable in the short term (given the production base). We therefore expect the government to target policies at growing the export base of Ghana to sustain foreign currency generation. We believe this will support the long term stability of the Cedi.

ANALYST CERTIFICATIONS AND REQUIRED DISCLOSURES BEGIN ON PAGE 3.

RESEARCH CONTACTS

Alex Boahen
alex.boahen@databankgroup.com
0302-610610 Ext 1600

Afua Dankwa Mensa-Bonsu
afua.mensa-bonsu@databankgroup.com
0302-610610 Ext 1602

Lawrencia A. Asante
afua.asante@databankgroup.com
0302-610610 Ext 1601

Jesse Opoku-Asiedu
jesse.opoku-asiedu@databankgroup.com
0302-610610 Ext 1601

Michael Asafo-Boakye Jnr.
michael,asafo-boakye@databankgroup.com
0302-610610 Ext 1604

Courage Kingsley Martey
courage.martey@databankgroup.com
0302-610610 Ext 1605

Courage Kwesi Boti
courage.boti@databankgroup.com
0302-610610 Ext 1603

SALES AND TRADING CONTACTS

Armah Akotey
armah.akotey@databankgroup.com
0302-610610 Ext 1700

Equities

Nene Nartey
nene.nartey@databankgroup.com
0302-610610 Ext 1702

Sidney Koranteng
sidney.koranteng@databankgroup.com
0302-610610 Ext 1703

Fixed Income

Edwige Yamoah
edwige.yamoah@databankgroup.com
0302-610610 Ext 1701

Davida Nyako
davida.nyako@databankgroup.com
0302-610610 Ext 1705

OFFICES

Head Office:
61 Barnes Road Adabraka,
PMB MPO, Accra,
Ghana
Tel : (+233 -302) 610 610
Fax : +233 (0)30 268 1443
Email: research@databankgroup.com

Kumasi Office:
Databank Brokerage Ltd,
Retail Services Division
House of Excellence – Adum,
Kumasi
PMB Central Post Office – Adum, Kumasi
Tel: (+233-3220) 81483, 80077
Email: kumasi@databankgroup.com

Tema Office:
Meridian Plaza, Room 201 & 202,
2nd Floor, Community 1,
Tema
Tel: (+233- 303) 213240, 210050
Fax: (233-303) 203438
Email: tema@databankgroup.com

Takoradi Office:
SSNIT Office Complex,
1st Floor, Room 208
Takoradi
Tel: (+233- 3120) 23628, 25465
Fax: (233-3120) 21653, 25075
Email: info@databankgroup.com

Banjul Office:
2nd Floor, Trust Bank Building,
Westfield Junction,
P.O Box 3189, Serrekunda,
The Gambia
Tel: (+220) 4378014,
Fax: (+220) 4378016
Email: gambia@databankgroup.com

Monrovia Office:
One Urban Plaza,
Tubman Boulevard Sinkor,
Monrovia, Liberia

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Databank | 61 Barnes Road, Adabraka | PMB MPO, Accra, Ghana | T: +233 (0) 302 610610 | F: +233 (0) 302 681443 | research@databankgroup.com