GHANA

UNDER PRESSURE

In Ghana, the warning signs are multiplying. Although economic growth has been fairly resilient, public finances have deteriorated sharply at a time of surging inflation. This is unsettling investors and threatening economic prospects. The central bank has already reacted by raising its key policy rate. But the authorities must reassure that they are capable of reducing the fiscal deficit. For the moment, they have failed to do so. Yet severe financial constraints and a dangerously high debt burden could force them to make adjustments.

The economy has entered a zone of high turbulence that risks undermining growth prospects, which had been fairly upbeat until recently. In addition to potential sanitary risks (only 7% of the population has been fully vaccinated), Ghana must now face up to the severe mistrust of investors. Unlike most of its regional peers, Ghana's sovereign spreads have widened abruptly, increasing 430 basis points (bp) to above 1,100 bp since October (chart 1). Such a high risk premium makes accessing the international financial markets prohibitively expensive, and the country is currently shut out of them. The cedi has also come under pressure in recent months, ending the year 2021 down 6% on the US dollar, one of the worst performances of the African currencies. Moreover, the upturn in financial tensions is occurring in the midst of an inflationary surge. In November, inflation hit 12.2%, the highest rate in more than four years. In response, the central bank raised its key rate by 100 bp to 14.5%. More key rate increases could follow in 2022. Yet the tightening of monetary policy is unlikely to have more than a limited impact on macroeconomic stability, unless it is accompanied by tangible progress on fiscal consolidation. That promises to be a major challenge.

FRAGILE CONSOLIDATION OF PUBLIC FINANCES

With a total fiscal deficit still estimated at more than 12% of GDP (due to the impact of the pandemic) and debt amounting to 80% of GDP in 2021, the fiscal consolidation programme presented in November was expected. Yet despite its ambitious targets, it proved to be unconvincing. The government intends to reduce the deficit to 7.4% of GDP in 2022 and 5.5% in 2023 before bringing it below the 5% threshold as of 2024. The primary balance should swing into positive territory as of 2022, after a deficit of more than 5% of GDP in 2021. Yet there are numerous doubts about how these targets will be met.

Revenues are supposed to increase by 43% in 2022, which is three times faster than nominal GDP growth. This assumes that new taxes will be introduced and tax collection will improve substantially. Yet with fiscal resources (excluding donor funds) levelling off at 14-15% of GDP for the past decade, Ghana has one of the narrowest tax bases in sub-Saharan Africa. In addition, the main budget measure (a 1.75% tax on digital transactions, which is supposed to generate 35% of the additional revenues anticipated by the government) has not been voted on yet, due to profound disagreements with the opposition party, which has the same number of parliamentary seats as the presidential party. Even if the measure is passed, however, it remains uncertain how much revenue it will actually generate.

The 2022 budget is also expansionary, with a planned 25% increase in spending to 27% of GDP, 8 points more than the pre-pandemic level of 2019. The planned slowdown in spending as of 2023 will thus begin from historically high levels. Moreover, fiscal slippage cannot be excluded given the acceleration of inflation, especially for public-service wages, which already absorb 40% of fiscal resources. Contingent liabilities will

FORECASTS

	2019	2020	2021e	2022e	2023e
Real GDP growth (%)	6.5	0.4	5.2	4.7	4.5
Inflation (CPI, year average, %)	8.6	9.9	10.0	9.0	8.8
Gen. Gov. balance / GDP (%)	-5.6	-13.8	-12.6	-9.4	-8.0
Gen. Gov. debt / GDP (%)	61.1	76.4	80.3	83.5	84.1
Current account balance / GDP (%)	-2.7	-3.1	-3.7	-3.5	-3.4
External debt / GDP (%)	38.9	45.5	47.0	46.9	47.5
Forex reserves (USD bn)	6.6	7.0	8.5	8.1	8.3
Forex reserves, in months of imports	2.9	3.4	3.9	3.6	3.6

TABLE 1
e: ESTIMATE & FORECASTS
SOURCE: BNP PARIBAS ECONOMIC RESEARCH

SOVEREIGN BOND SPREADS

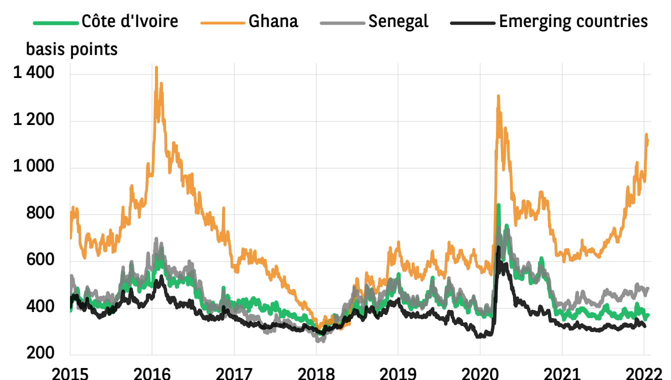

CHART 1
SOURCE: JP MORGAN

also remain a risk, although they have tended to decline since banking sector restructuring was completed (it had a cost of about 8 points of GDP between 2017 and 2021). However, shortages in the energy sector could also generate extra costs for the government of up to 2 points of GDP per year.

DANGEROUSLY HIGH DEBT BURDEN

It is thus highly unlikely that the authorities will meet their fiscal targets in the short and medium term, unless they are forced to comply. We expect a higher budget deficit than the government's forecasts (9.4% of GDP in 2022, 8% in 2023, *cf.* chart 2), which means the debt ratios will

continue to deteriorate, at least for the next two years. At 84% of GDP at year-end 2023, public debt would swell to dangerously high levels. Moreover, its structure makes it vulnerable to multiple shocks, such as a sharper than expected growth slowdown in the emerging countries, especially in China, or the tightening of US monetary policy.

At mid-2021, non-resident investors held nearly 20% of domestic debt, the equivalent of USD 5.8 bn, compared to foreign reserves of less than USD 9 bn. As a result, despite a moderate current account deficit and an export base whose price trends are rarely synchronised (gold accounted for 47% of exports in 2020, oil for 20% and cacao for 16%), Ghana is still exposed to major capital outflows with potentially strong pressures on the exchange rate. In addition, nearly half of its public debt is denominated in foreign currency; the debt ratio automatically increases by 4 points of GDP with every 10% depreciation of the cedi.

The deterioration in external financing conditions would not be limited to pressures on external liquidity. The government plans to cover 80% of its financing needs on the domestic market. But with total bank assets accounting for 40% of GDP, the financial market is rather small. Moreover, banks are already rather highly exposed to sovereign risk. At the end of June 2021, government loans outstanding accounted for 46.5% of banking system assets, compared to 37.5% at year-end 2019. In the absence of an alternative to funding from the international market, the authorities may have to turn to the central bank again. In 2020, a monetisation programme equivalent to 2.6% of GDP helped cover a quarter of the government's domestic financing needs. However, the central bank's policy rate increase in November seems to indicate that monetary stability is being given priority again. It also risks increasing even more the already very expensive cost of government borrowing. Treasury bond rates fluctuate between 16% and 19% for maturities of 1 to 3 years. Interest payments already absorb nearly half of fiscal resources, 80% of which is for locally-issued debt instruments. The government's manoeuvring room is all the narrower since it must refinance 42% of the domestic debt over the next three years. Fortunately, the next major Eurobond does not mature before 2025.

ECONOMIC GROWTH IS BOUND TO SLOW

So far, economic activity has held up fairly well. The economy managed to escape recession in 2020, and the figures for the first 9 months of 2021 were surprisingly favourable, with average growth of 5.3%, thanks to a strong rebound in the services sector. The government's forecast of 4.4% made as part of its budget presentation is likely to be exceeded.

In contrast, the official 2022 growth forecast of 5.8% seems to be extremely optimistic. We rather expect economic growth to slow to 4.7% due to the tightening of financing conditions and monetary policy. The authorities are notably calling for a 29% increase in public investment in 2022. However, it is highly probable that the latter will serve as an adjustment variable. Another constraint stems from the persistence of major fiscal deficits.

In the banking sector, the loan-to-deposit ratio has fallen to a historically low level of 52%, nearly 10 points less than at year-end 2019. In a fragile economic environment, Ghana's banks will tend to favour the safer government securities. Yet with a non-performing loan ratio of 16.4% in November (14.3% at year-end 2019), credit risk is high. Moreover, the tightening of monetary policy will continue to deteriorate lending conditions and will further strain the growth of bank lending to the private sector, which was already negative in real terms at the end of November (-0.8%).

FISCAL AND DEBT INDICATORS

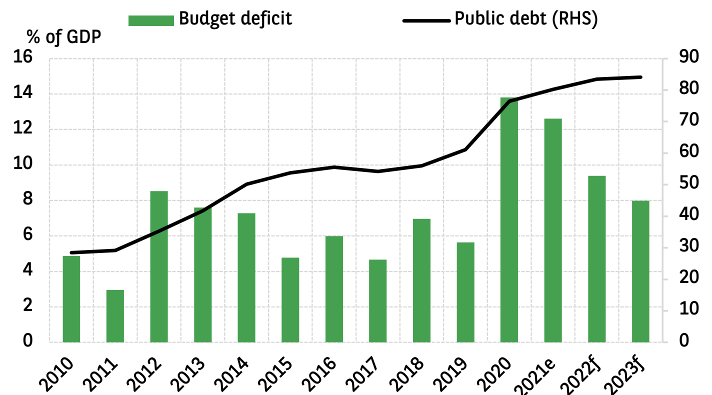

CHART 2

SOURCE: MOF, BNP PARIBAS

Looking beyond Ghana's economic growth momentum, the main source of concern is the risk of a new episode of macro-financial stress. In 2015, after the cedi had declined by nearly 50% against the USD in two years, the authorities decided to sign a funding agreement with the IMF. For the moment, the authorities do not think they will need to call on this assistance, but the warning signals are multiplying.

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