



## **Our Mission**

To maintain Stability in the General Level of Prices  
To promote Efficient Operations of the Banking and Payment  
Systems and Economic Growth.

# ***MONETARY POLICY FRAMEWORK IN GHANA: PRACTICE AND CHALLENGES***

***Presentation by  
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Practice and Challenges***

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■ Our mission is to pursue sound monetary and financial policies aimed at price stability and create an enabling environment for sustainable economic growth.



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# Outline

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- Monetary Policy in Ghana
- Case for review and choice of framework
- Key Economic Performance Indicators in Ghana
- Monetary policy challenges and prospects
- Summary and Conclusions



# Monetary Policy in Ghana .....

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- Control regime - Direct Instruments (prior to 1992)
- Monetary Targeting - Indirect Instruments (1992 – 2002)
- Inflation Targeting - Indirect Instruments (since 2002 but the formal announcement was made in 2007)
  - ✓ The New Bank of Ghana Act ( Act 612)
  - ✓ The MPC Framework



# Case for the current Framework....

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- The policy arena became primarily characterised by:
  - High and volatile inflation and exchange rate depreciation
  - Strong fiscal dominance in which persistent fiscal deficits were financed largely by monetary accommodation
- Ineffectiveness of the nominal anchor (instability of the velocity with financial market liberalisation and structural change)
- Anchoring economic agents' inflation expectations also became difficult or impossible.
  - partly reflecting the high and volatile inflation and exchange rate depreciation episodes



# Choice of the current Framework....

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- Current framework was designed to engineer a switch to low inflation and exchange rate stability, through increased coordination with fiscal policy.
- Monetary policy was explicitly to achieve price stability, **operationalized through the adoption of an inflation targeting regime in 2002, but formal announcement was made in 2007.**



# Choice of the current Framework....

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- **A new BOG Act, 2002, (Act 612)** set the tone for IT in Ghana:
  - “The primary objective of the Bank is to maintain **stability in the general level of prices**” (Section 3, subsection 1).
  - “Without prejudice to the above, the Bank shall support the general economic policy of the Government and promote economic growth and effective and efficient operation of banking and credit systems in the country, **independent of instructions from the Government or any other authority**” (Section 3, subsection 2).
- ***The new Act thus granted the Bank operational independence.***



# Choice of the current Framework....

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- The Act tackles the issue of fiscal dominance through:
  - Placing a limit on government's borrowing in any fiscal year (**Section 30, sub-section 2**) and
- Provides for the establishment of a Monetary Policy Committee (MPC) (**Section 27**)



# Choice of framework in Ghana....

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- Aside from the institutional reforms, a number of technical studies were conducted as to the most appropriate options available including:
  - A re-examination of the money demand function and
  - Studies on the channels of monetary transmission mechanism





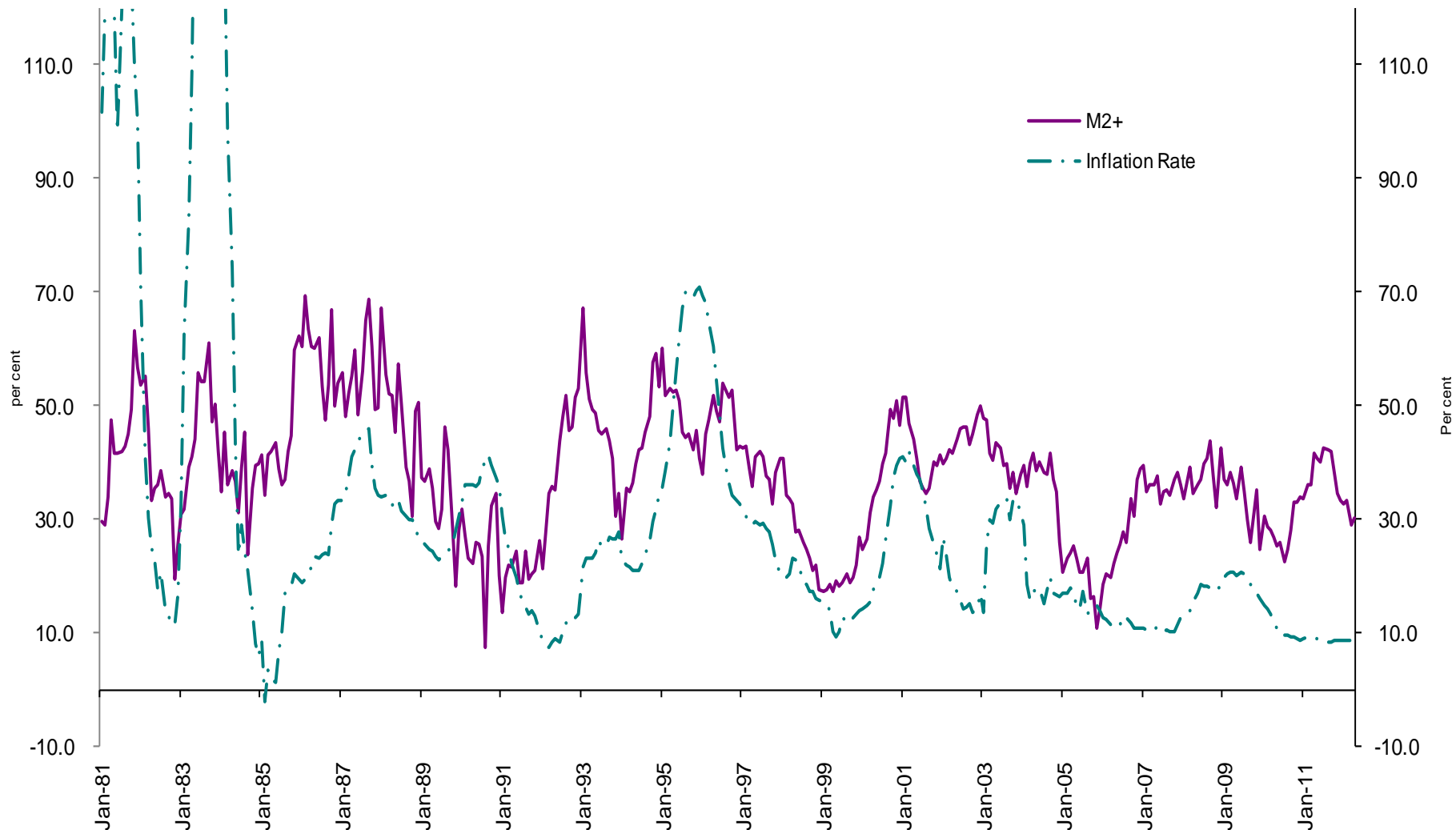
# Choice of framework in Ghana....

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- The re-examination of the money demand function necessitated by observation of high and volatile monetary growth, that occasionally overshoot targets, while inflation remained low and stable.
- The paper concluded that evidence from the statistical and econometric methodologies showed parametric shifts in the demand for money function (following the period of steady structural reforms and financial sector deregulation).



# Ghana: money and inflation (Jan 1981 – Apr 2012)



# Choice of framework in Ghana....

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- This finding had an important implication for viability of framing monetary policy around monetary aggregates
  - Implied money growth rates alone were not good predictors of future inflation and real output.
- ...and provides support for the current policy regime (IT)
  - where several indicators are considered in taking monetary policy decisions rather than only money supply.
- A recent study (2011) on Ghana by the IMF arrived at the same conclusion (WP/11/274).



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# ***Practical aspects of implementation of inflation targeting in Ghana***



# The MPC Process...

- Membership:
  - 7 members; 5 internal, 2 external members
  - Chaired by the Governor, who has a vote
  - Members independent in the decision process
  - Currently, decisions are by consensus
  - MPC sets interest rates (the Bank of Ghana Policy rate)
    - But may also use other instruments

## *Typical MPC Session*



# The MPC Process....

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Meetings: Bi-monthly meetings during which the MPC examines reports covering:

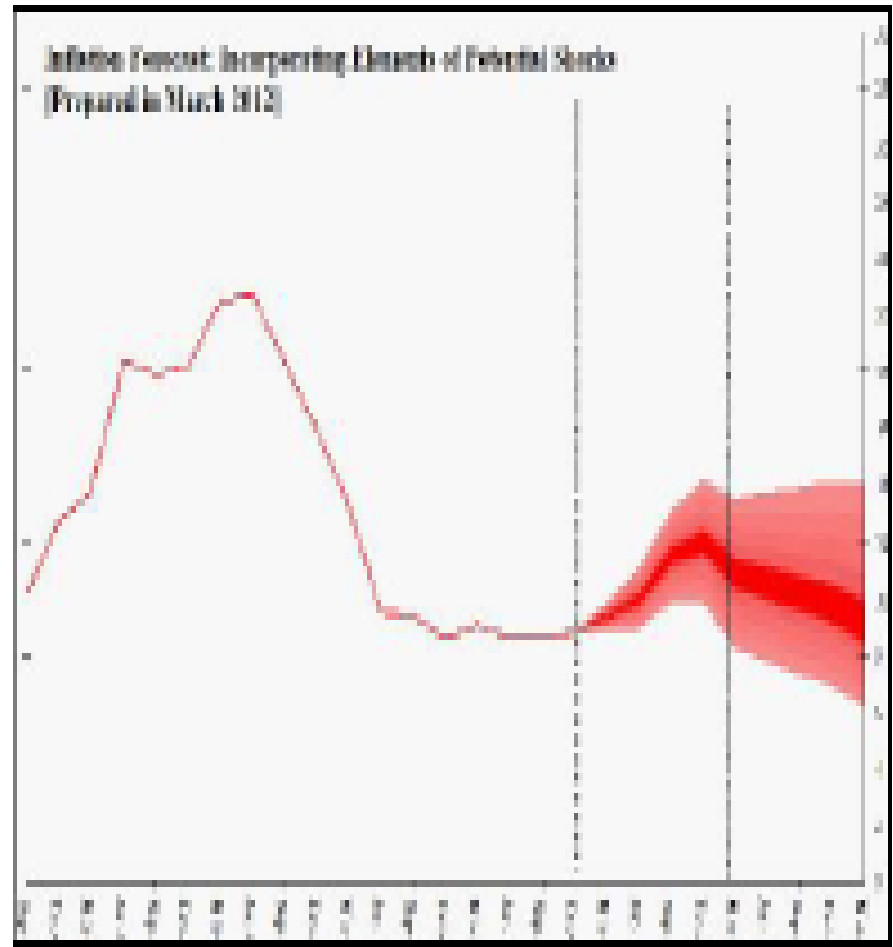
- WEO & Global Monetary Policy Stance
- Real sector developments (Composite index of Economic activity; business and consumer confidence surveys etc.)
- Bank of Ghana Urban Index
- Financial stability reports (Banking sector, stress tests and credit conditions survey)
- Fiscal developments
- Monetary and financial developments
- External sector & Balance of Payment developments



# The MPC Process.....

## ...Meetings continued...

- Inflation outlook and analysis
  - *Fan Chart Forecast*
- Available information is summarized into a matrix of risk assessment and an inflation risk measure is derived from the matrix.



# The MPC Process.....

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## *Transparency and communication*

- Pre-announced meeting dates
- Press releases
- Bank of Ghana Monetary Policy Reports
- Publication of Annual percentage rates (APRs)
- Monetary Policy lectures by MPC Members and staff
  - ✓ (e.g. educational institutions, press, business community, etc.)



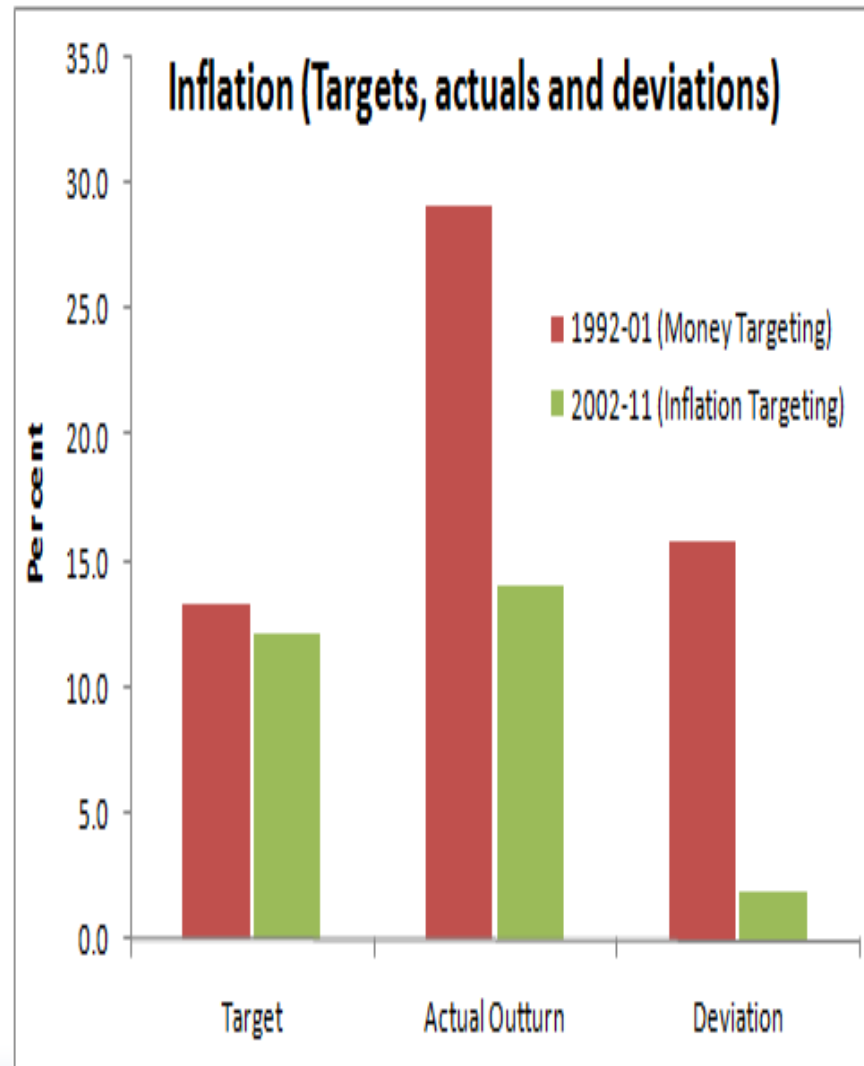
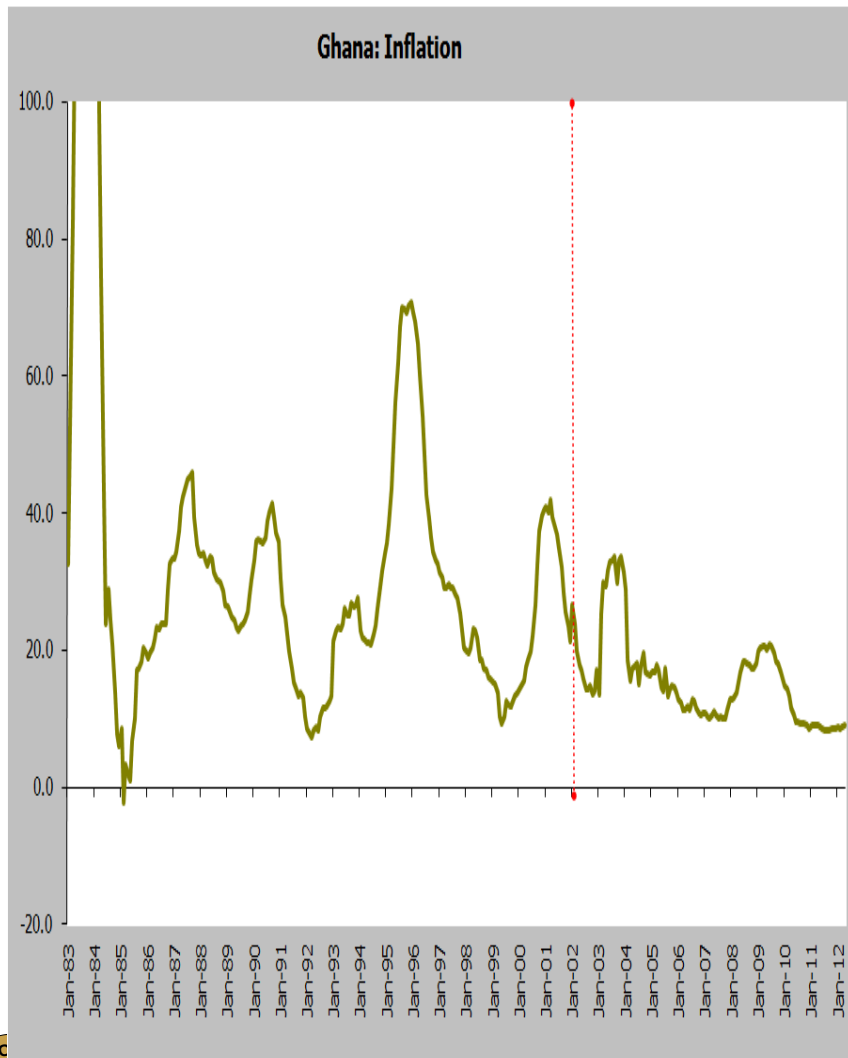


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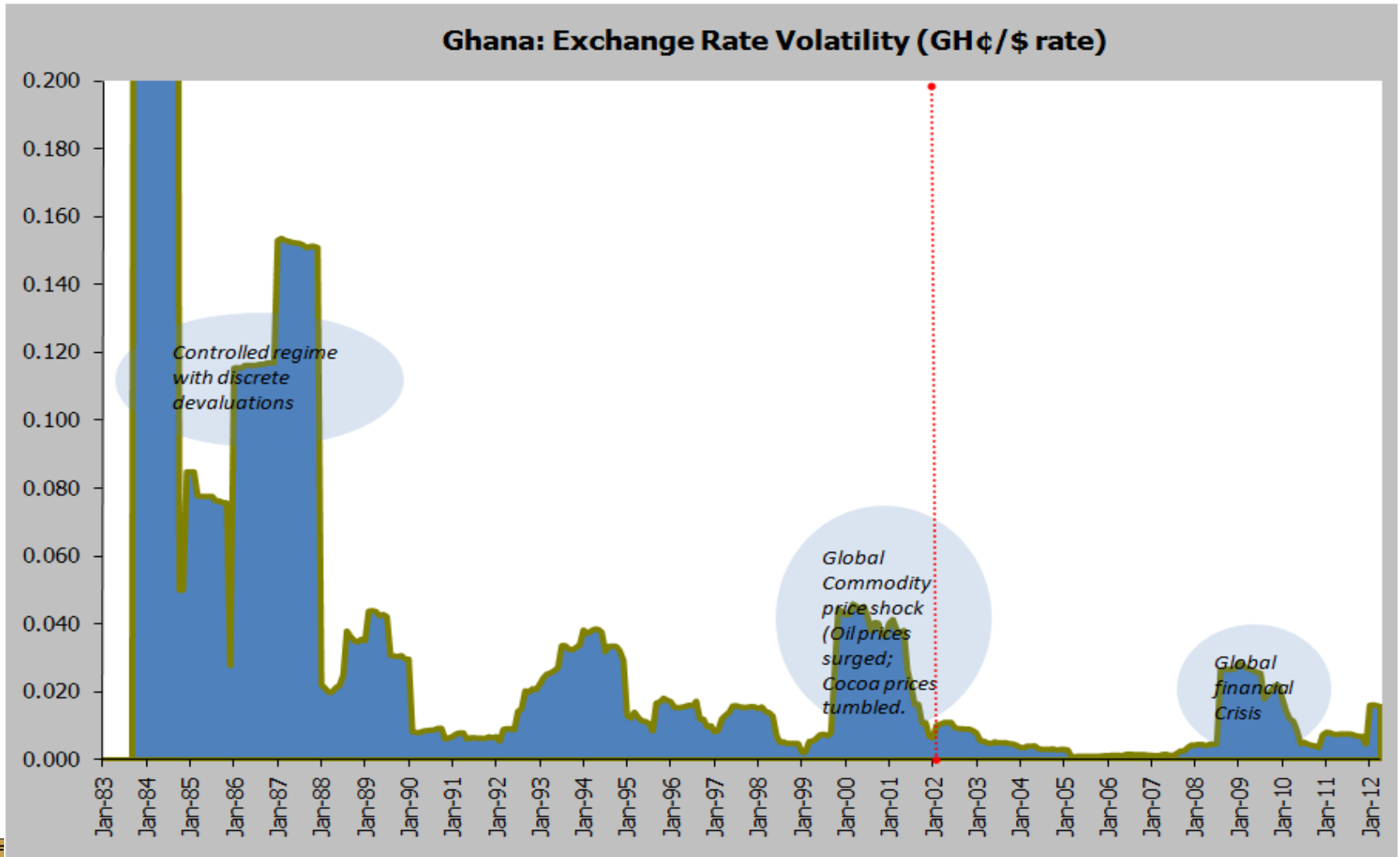
# *HISTORICAL ECONOMIC PERFORMANCE*



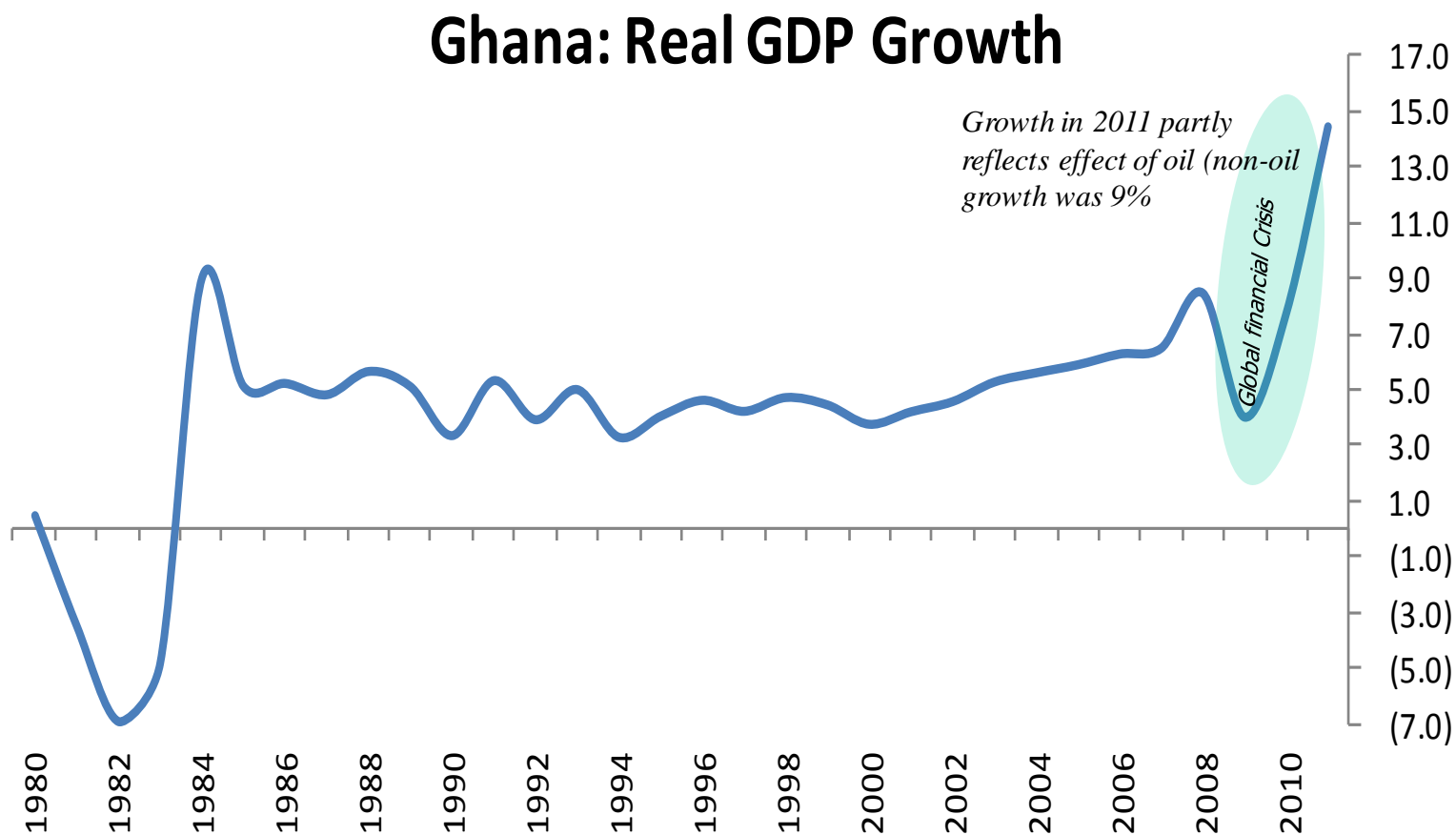
# Broadly reduced inflation that has generally remained on target with minimal deviations



# Significantly reduced exchange rate volatility; but effects of global shocks remain noticeable even if muted



Relatively strong Real GDP growth over the last decade with noticeable slowdown following the global economic meltdown



*Ghana remains a favourable destination for capital inflows; portfolio flows are high relative to other peer countries and occasionally complicates macroeconomic management*

***Private capital flows (net) to selected peer countries***

	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>
<b>South Africa</b>	10,420	13,515	12,997	(2,538)	15,664	11,654
<b>Nigeria</b>	4,480	6,120	6,364	1,729	5,459	7,729
<b>Ghana</b>	145	702	2,010	2,054	1,634	3,148
<b>Zambia</b>	479	666	1,366	933	620	826
<b>Mozambique</b>	19	30	425	584	883	791
<b>Uganda</b>	366	666	837	746	624	707
<b>Tanzania</b>	938	406	584	403	418	437
<b>Seychelles</b>	79	336	272	121	244	362
<b>Mauritius</b>	(21)	67	340	156	135	118
<b>Kenya</b>	(19)	6	668	26	74	#N/A
<b>Sierra Leone</b>	91	59	97	59	80	67
<b>Total</b>	<b>16,977</b>	<b>22,573</b>	<b>25,960</b>	<b>4,273</b>	<b>25,835</b>	<b>25,839</b>

*Source: World Bank, World Development Indicators and Global Development Finance*



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# CHALLENGES



# *There are a number of Challenges including .....*

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- Sterilizing capital inflows (cost)
- Destabilizing effects of portfolio flows
  - Reflecting opportunities elsewhere
- Data challenges
  - High frequency data
- Transparency issues
  - Publication of minutes
- Transmission mechanism
- Policy coordination with fiscal, foreign exchange and money market still being streamlined



# Other challenges for MP in Ghana

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- Openness to trade and recurrent external shocks
  - Cocoa and gold account for about 60 percent of export proceeds
  - Commodity imports /GDP per cent is about 43
- Seasonality of cocoa flows
- Capacity building
- Conflict with BOG Board





*More reforms being undertaken to improve process and also enhance efficiency of the transmission mechanism of monetary policy.....*

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- Credit reporting bill and establishment of credit reference bureaus
- Payments systems reform
- Collateral enforcement
- etc



# CONCLUSIONS

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- MP is a dynamic process and occasionally adjusted to reflect prevailing conditions.
- Ghana adopted the IT framework since 2002 and has significantly reduced both the rate of inflation and inflation expectations.
  - However, it is also true that the past decade has generally been associated with low levels of inflation.
- Nevertheless, challenges remain, including long lags in transmission process, vulnerability to external shocks, etc
- Accompanying institutional and money market reforms are important to underpin the MP transmission process.



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# Thank You for Your Attention

