



Bank of Ghana Monetary Policy Report

Inflation Developments and Outlook

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1.0 Overview of Developments in the Third Quarter, 2011

“ Global growth is forecast to regain some momentum during the second half of 2011. Real GDP growth in the advanced economies is expected to rebound. Growth is expected to remain elevated in emerging Asia, notably in China and India, followed by sub-Saharan Africa.”

Global economic growth over the 11-month period has weakened and become more uneven as the sovereign debt crises affecting the Euro-zone area threatens to engulf more countries. Against this backdrop, progress in rebuilding macroeconomic buffers after the financial crises has slowed in most Low Income Countries' (LICs). There is currently a real risk of downturn in global economic recovery, commodity price shocks and high food prices.

The outlook for the global economy continues to be uncertain with weak growth and declining consumer confidence. There is continuing anxiety regarding the sovereign debt problem in the Euro zone and together with the slower-than expected growth in the U.S., these have intensified downside risks to global recovery.

Growth in emerging and developing economies was fairly robust. In Sub-Saharan Africa, economic growth was supported by increased exports and relatively stable financial systems.

High levels of unemployment and slow economic recovery contributed to the decline of headline inflation in major advanced economies. However, inflation was a major concern for emerging and developing countries in the early part of the year, due largely to rising commodity prices, especially in food and fuel. After initially rising steeply, commodity prices have since been on a downward path. Consequently, inflation levels have eased in some emerging and developing countries.

On the domestic economy, the following conditions were observed:

- Since the meeting in October 2011, the Ghana Statistical Service has released two inflation reports. The rate of inflation which settled at 8.4 percent at the end of the third quarter marginally increased to 8.6 percent in November 2011.
- Inflation remained within single-digits during the year. From 9.1 per cent in January, it declined to 8.4 per cent at the end of the third quarter but has since inched up to 8.6 per cent in November. Food Inflation which stood at 4.8 per cent in January 2011 declined to 4.4 per cent by the end of November 2011. Similarly, non-food inflation fell from 11.8 per cent to 11.1 per cent over the same period.
- Core inflation, which measures underlying inflation, dropped from 8.1 per cent in January 2011 to 7.5 per cent in June 2011, but has increased to 7.9 per cent in November 2011.
- The latest Consumer Confidence Survey, conducted by the Bank of Ghana in November 2011, showed a decline in the index from 103.6 in September to 99.3. Factors cited by respondents for the decline in confidence include the uptick in inflation and pressures on the Cedi.
- The Bank of Ghana's Composite Index of Economic Activity (CIEA) indicates continued momentum in economic activity. The CIEA recorded a 6.4 per cent growth between August and October 2011. On a year-on-year basis, the CIEA posted a growth of 18 per cent. The increase was reflected in growth in all the indicators of the Index.
- Provisional data on the implementation of the government budget indicates that total revenue and grants for January to November 2011 increased to GH¢9.3 billion from the GH¢6.4 billion recorded for the same period in 2010. Also, total expenditure (excluding foreign financed capital expenditure) for the first eleven months of 2011 amounted to GH¢11.5 billion compared to GH¢8.2 billion a year ago.
- Fiscal operations during the period, therefore, resulted in a narrow budget deficit of GH¢2.2 billion. The deficit, together with a net foreign loan repayment of GH¢132.7 million, was financed by a net domestic borrowing of GH¢2.4 billion.

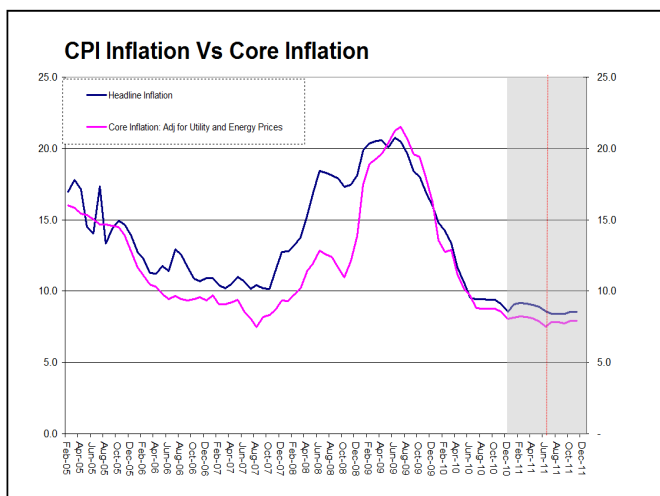
- Total merchandise exports increased to US\$11.8 billion in 2011, representing a growth of 64.7 per cent over the value for the same period in 2010. The strong export growth was driven by gold and cocoa beans with a boost from crude oil. Also, total merchandise imports since the beginning of 2011 amounted to US\$14.4 billion, representing an annual growth of 49.9 per cent. The resulting balance of trade data therefore, shows a provisional deficit of US\$2.6 billion for the first eleven months of 2011 compared with US\$2.4 billion for the corresponding period in 2010.
- Developments in the nominal bilateral exchange rates of the cedi to the US dollar showed increased depreciation. In the year to November 2011, the cedi depreciated by 4.5 per cent against the US dollar, compared with a depreciation of 0.6 per cent in November 2010. In trade weighted terms, a real effective depreciation of 2.3 per cent was recorded in November 2011, compared to an appreciation of 1.5 per cent in the corresponding period of 2010.

2.0 Inflation Developments through November 2011

“Price developments in the domestic economy indicate that the consumer price index has changed very little in the past three months to November 2011”

Annual CPI inflation for November 2011 was 8.55 per cent, down marginally from 8.56 per cent in October 2011. The November inflation outturn was 0.53 percentage points lower than that of the corresponding period in 2010. The principal factors that have supported stable inflation conditions include stable exchange rate and favourable food supply conditions. However, there has been a reversal in the declining trend in food inflation starting from February 2011. Food inflation has subsequently increased to 4.41 per cent in November 2011, up from 4.03 per cent in October 2011. The food inflation in November 2011 was however, far lower compared to the 5.32 per cent recorded for the same period in 2010. The Non-Food inflation on the other hand, dropped marginally by 0.24 percentage point to 11.08 per cent in November 2011. It also compares favourably with 11.5 per cent recorded in the corresponding period a year ago.

The monthly inflation rate picked up marginally in November 2011. The overall monthly inflation inched up to 0.46 per cent in November 2011 from -0.8 per cent in June. The November 2011 monthly inflation compares favourably with 1.01 monthly inflation recorded in a similar period a year ago.



Developments in the sub-groups of the consumer basket produced mixed outcomes in November 2011. While Fruit and vegetables including potatoes and others sub groups' inflation eased to drive down the overall inflation, inflation in the remaining sub groups picked up significantly.

3.0 The Outlook and Assessment of Risks to CPI Inflation

The risks to inflation seem fairly balanced at this stage. All the macroeconomic indicators seem to be pointing in the right direction and the expectations are that this will continue, keeping inflation fairly stable.

Inflation forecast from the beginning of the year suggested a relatively stable inflation profile for both the first and the second half of the year. Forecasts indicate that end year inflation target of 8.7 percent is likely to be achieved. However looking forward to 2012, there are both upside and downside risks to inflation. An examination of the key macroeconomic fundamentals show that most of the indicators do not show any significant deviation that signify the emergence of inflationary pressures (see table 1).

	Dec-09	Dec-10	Jan - 11	Feb-11	Mar-11	Apr-11	May-11	Jun-11	Jul-11	Aug-11	Sep-11	Oct-11	Nov-11
1 Inflation (per cent)													
CPI Year-on-Year	16.0	8.6	9.1	9.2	9.1	9.0	8.9	8.6	8.4	8.4	8.4	8.6	8.6
CPI Yearly Average	19.3	10.7	11.5	10.8	10.0	10.4	9.8	9.1	9.6	9.3	9.4	9.2	8.9
CPI Month-to-Month	1.6	1.1	2.1	1.6	1.1	1.3	1.8	1.3	0.6	-0.7	-1.5	-0.8	0.3
2 Crude Oil Prices (\$ per barrel)													
	72.2	78.3	111.4	115.7	124.1	123.1	114.5	113.9	117.0	108.8	110.0	110.0	110.6
5 Interest Rates													
Monetary Policy Rate	18.0	13.5	13.5	13.5	13.5	13.5	13.0	13.0	12.5	12.5	12.5	12.5	12.5
91 - day T Bill Rate	23.7	12.3	12.2	12.1	12.1	12.1	11.2	10.3	10.4	9.4	9.4	9.3	9.3
182 - day T Bill Rate	26.5	12.7	12.6	12.5	12.5	12.5	11.9	10.7	11.2	10.1	10.1	9.9	10.2
6 Exchange Rate (GHC/US\$)													
Year to Date Depreciation()/Appreciation(=)	1.4284	1.4738	1.5013	1.4937	1.5021	1.4972	1.5018	1.5064	1.5055	1.5104	1.5224	1.5326	1.5309
	15.0	3.1	1.8	1.3	1.9	1.6	1.9	2.2	2.1	2.4	3.2	3.8	4.3
7 Money Supply (M2+)													
Year to Date Depreciation()/Appreciation(=)	10,240.9	13,775.4	13,751.3	13,808.1	14,168.3	14,817.4	14,846.7	15,202.1	15,353.9	15,388.6	15,851.2	16,929.1	N/A
Growth (yr-on-yr)	25.0	34.5	32.8	35.3	35.5	40.1	30.4	40.2	42.6	42.1	41.9	38.1	N/A
8 Gross Reserves (US\$m)													
Months of Import Cover	3,167.1	4,680.0	4,767.8	4,825.5	4,503.6	4,883.0	4,704.5	4,764.9	4,629.2	4,502.0	4,594.7	4,977.6	4,845.8
	3.0	3.7	3.8	3.8	3.5	3.8	3.7	3.7	3.6	3.5	3.5	3.0*	2.9*
9 Total Debt													
Domestic	13,258.2	17,392.2	17,428.4	18,296.8	18,553.5	19,820.1	20,129.9	21,352.2	21,627.6	22,311.9	22,245.9	22,770.8	23,431.8
External (US\$m)	6,103.0	8,280.1	8,413.5	8,829.6	8,839.6	9,606.6	9,998.0	10,795.1	10,870.1	11,388.1	11,432.1	11,562.0	11,697.0
Total debt % of GDP	5,007.9	6,251.6	6,379.4	6,439.2	6,681.9	6,749.1	6,745.9	7,008.2	7,145.5	7,232.4	7,103.1	7,313.6	7,613.5
	36.0	37.8	31.7	32.5	33.2	34.7	35.4	30.8	40.5	41.8	41.7	42.6	43.9
10 Fiscal (Narrow Deficit)													
Balance	-2,056.2**	-2,099.0**	102.9	-287.7	-641.7	-214.1	-312.2	672.9	-424.8	-139.5	-33.5	-463.2	-552.8
Cumulative			105.9	-181.8	-823.5	-1,037.6	-1,349.8	-701.9	-1,130.3	-1,269.8	-1,287.8	-1,716.6	-2,240.5
% of GDP	-9.2	-6.8	0.2	-0.3	-1.5	-1.9	-2.5	-1.2	-2.1	-2.4	-2.4	-3.2	-4.2
NDF	1,012.1	2,143.0	88.9	15.6	675.2	253.0	376.1	626.8	145.5	197.0	104.3	490.8	618.1
Cumulative			-88.9	-104.5	570.6	835.6	1,201.7	599.8	1,045.9	1,243.0	1,329.8	1,784.0	2,373.2

Notes
* Based on revised average monthly imports of goods and services for 2012
** Broad Budget Balance

The table point to the following:

- A stable Inflation profile observed in 2011 up to November 2011
- A rise in the average price of crude oil from US\$78.3 per barrel in December 2010 to US\$110.6 as at November 2011
- A decline in interest rate (91-day Treasury Bill) from 12.3 percent in December 2010 to 9.3 percent by November 2011
- An acceleration in the rate of depreciation of the currency; from 1.8 percent to 4.3 percent by November 2011
- A slight increase in money supply growth from 34.5 percent at the beginning of the year to 38.1 percent by October 2011
- A slight build-up in reserves from US\$4.7 billion to US\$4.8 billion
- A provisional overall fiscal deficit of 4.2 percent of GDP for November 2011 compared with a deficit of 6.8 percent attained in 2010

While general macroeconomic conditions look favourable, there are however certain risks that are beginning to emerge which could affect the profile in the short-to-medium term. Both upside and downside risks to inflation exists.

The upside risks include the following:

- The Exchange rate volatility observed in the fourth quarter of 2011 and its impact on pricing behaviour of economic agents over the horizon. Taking the lagged impact effect of exchange rate movements and impact on prices, the impact effect is expected to be felt in prices by the end of the second quarter of 2012.
- There was also some risks emerging from the Balance of Payments. Indications from the foreign exchange market suggested increased demand for oil and non-oil imports. This indication meant that the Balance of Payments was expected to deteriorate in 2011 and exert further pressures on the exchange rate.
- At the last MPC meeting in October 2011 MPC the indication was that given the trends in the international price movements of crude oil, domestic petroleum prices were bound to increase. A maximum increase of 25 percent in petroleum prices was factored in the analysis. This was also a potential source of inflationary pressure in the outlook given the historical impact of such increases.

The pass-through effect to transportation costs, food prices and non-food prices is expected down the line in the first half of 2012.

- Wage pressures is also a source of concern in the outlook. In October 2011, it was observed that organised labour were beginning to agitate to pay increases. The fact that the economy was entering into another phase of the business cycle in 2012 meant that these agitations would intensify in 2012. In addition, the full execution of the arrears clearance and the single spine pay policy are all expected to add up to aggregate demand pressures in the outlook.
- The surge in monetary aggregates also posed some concern in the outlook. Money supply growth was as high as 38 percent in November 2011 driven mainly by increases in the Net Foreign Asset of the Bank of Ghana. While the explanatory role of money and its impact on inflation may have diminished in the economy, its role still matters as far as the inflation-growth nexus in the economy is concerned.
- Businesses inflation expectations are becoming dislodged. Recent surveys show that businesses expect inflation to rise in the next year. This may influence the pricing behaviour of businesses in the months ahead and could affect inflation.
- Most forecasts show the world economy heading for a slowdown in 2012. The impact of the slowdown in the world economy will have implications for commodity prices and result in worsened terms of trade conditions. From the fiscal point of view revenue from cocoa, gold and oil will drop and this will also exert some pressure on the fiscal.

The downside risks could come from the following sources:

- As crude oil prices drop in response to the slowdown in the world economy the potential for domestic petroleum prices to fall exists. When passed on, CPI inflation could ease down somewhat.

- With weakness in the world economy, the projections show that foreign inflation is likely to fall in 2012 and 2013. The potential to import low inflation is a source of downside risk in the outlook.
- While Domestic VAT collections have increased in the first 10-months of the year, an analysis of the data shows that growth is below trend and remains slightly weak. Trends in Domestic VAT collections are used to serve as a proxy for measuring and gauging aggregate demand pressures. The fact that current trends are below trend implies weak aggregate demand condition, a situation that could help weigh down on inflation in the outlook if the current trends (negative gap) continues

In summary, while upside risks and downside factors to inflation exist, the outlook suggests that in 2012 there will be an interplay of these forces acting together to determine the outturn of inflation and growth. Although the indications suggest that the headwinds are for an upward trajectory in the inflation profile, the expected rise in inflation will not be significant enough to go beyond the upper band limit of 10.7 percent.

4.0 Conclusions

Ghana's provisional GDP growth was estimated to have improved from 7.7 per cent in 2010 to an estimated 13.6 per cent in 2011 on account of oil production. Inflation and inflationary expectations have however been firmly anchored while monetary growth over the review period have also edged up slightly. The external sector performance has been relatively strong underpinned by a vibrant exports sector. At the end of November 2011, Gross International Reserves was estimated at US\$4,845.8 million, enough to cover 2.9 months of imports of goods and services.

The rate of Inflation for 2011 has remained relatively stable since the beginning of the year through to the fourth quarter. However, there are signs of emerging risks to inflation which would have to be managed in the ensuing months. Looking ahead and factoring in all the upside and downside risks to inflation and growth, economic conditions are expected to remain stable.

Annexures:

A.1. 1 Developments in Headline Inflation

Table 1: Overall Inflation, Food Inflation and Non-Food Inflation									
	Dec-09	Dec-10	Mar-11	Jun-11	Jul-11	Aug-11	Sep-11	Oct-11	Nov-11
Overall Inflation Rates	16.0	8.6	9.1	8.6	8.4	8.4	8.4	8.6	8.6
Food Inflation	11.8	4.5	4.7	2.8	3.3	3.8	3.7	4.0	4.4
Non-Food Inflation	18.8	11.2	12.0	12.4	11.8	11.4	11.3	11.3	11.1

A1.2 Monthly Price Developments in the Overall Consumer Price Index

All - Items Consumer Price Index:																	
Monthly Price Movements (2007-2011)																	
Year	Jan	Feb	Mar	Q1 Avg.	Apr	May	June	Q2 Avg.	Jul	Aug	Sept	Q3 Avg.	Oct	Nov	Dec	Q4 Avg.	Annual Average
2007	1.1	1.2	1.3	1.2	1.5	1.8	0.7	1.4	1.2	0.2	-0.2	0.4	-0.2	1.6	1.8	1.1	1.0
2008	1.2	1.6	1.8	1.5	2.9	3.2	2.1	2.7	1.1	0.0	-0.4	0.2	-0.7	1.7	2.4	1.2	1.4
2009	2.6	2.0	2.0	2.2	2.9	2.8	2.6	2.8	0.9	-0.7	-1.5	-0.4	-0.9	0.8	1.6	0.5	1.3
2010	1.6	1.5	1.1	1.4	1.4	1.9	1.6	1.6	0.8	-0.7	-1.5	-0.5	-1.0	0.5	1.1	0.2	0.7
2011	2.1	1.6	1.1	1.6	1.3	1.8	1.3	1.5	0.6	-0.7	-1.5	-0.5	-0.8	0.5	NA	-0.2	0.7

A1.3 Monthly Price Developments in the Food Price Index

Food Price Index																	
Monthly Price Movements (2007-2011)																	
Year	Jan	Feb	Mar	Q1 Avg.	Apr	May	June	Q2 Avg.	Jul	Aug	Sept	Q3 Avg.	Oct	Nov	Dec	Q4 Avg.	Annual Average
2007	1.4	2.3	0.7	1.5	2.3	2.8	0.7	1.9	1.0	-1.1	-1.5	-0.5	-1.1	1.0	1.5	0.5	0.8
2008	1.5	2.9	2.3	2.2	2.5	5.2	2.3	3.3	0.8	-1.0	-1.9	-0.7	-2.8	1.8	2.3	0.4	1.3
2009	3.9	2.5	1.9	2.7	3.2	3.4	0.9	2.5	0.5	-1.3	-3.6	-1.5	-2.2	0.7	1.8	0.1	1.0
2010	1.3	1.6	1.1	1.3	1.7	2.3	2.3	2.1	0.2	-1.8	-3.3	-1.6	-2.2	0.5	1.0	-0.2	0.4
2011	1.6	1.4	1.2	1.4	1.2	2.0	1.1	1.5	0.7	-1.3	-3.4	-1.3	-1.9	0.8		-0.6	0.3

A1.4 Monthly Price Developments in the Non-Food Price Index

Non-Food Price Index																	
Monthly Price Movements (2007-2011)																	
Year	Jan	Feb	Mar	Q1 Avg.	Apr	May	June	Q2 Avg.	Jul	Aug	Sept	Q3 Avg.	Oct	Nov	Dec	Q4 Avg.	Annual Average
2007	0.9	0.4	1.7	1.0	1.0	1.1	0.8	0.9	1.3	1.1	0.7	1.0	0.5	2.0	2.0	1.5	1.1
2008	0.9	0.7	1.5	1.0	3.2	1.7	1.9	2.3	1.3	0.7	0.7	0.9	0.9	1.7	2.5	1.7	1.5
2009	1.8	1.7	2.0	1.8	2.7	2.4	3.9	3.0	1.2	-0.3	0.0	0.3	-0.1	0.8	1.5	0.7	1.5
2010	1.8	1.5	1.2	1.5	1.2	1.6	1.1	1.3	1.2	0.0	0.3	0.5	-0.2	0.5	1.2	0.5	0.9
2011	2.3	1.7	1.0	1.7	1.4	1.6	1.4	1.4	0.6	-0.3	-0.4	0.0	-0.1	0.3		0.1	0.9

A1.5 Trends in the Core Measures of Inflation

Ghana: Measures of Core Inflation															
	Dec-07	Dec-08	Dec-09	Mar-10	Jun-10	Sept-10	Dec-10	Mar-11	June-11	July-11	Aug-11	Sept-11	Oct-11	Nov-11	
Headline Inflation	12.7	18.1	16.0	13.3	9.5	9.4	8.6	9.1	8.6	8.4	8.4	8.4	8.6	8.6	
Core 1: Inflation excl Energy and Utility	9.4	13.9	16.2	12.9	9.7	8.8	8.0	8.2	7.5	7.8	7.8	7.7	7.9	7.9	
Core 2: Inflation excl Energy and Utility and Volatile Food Items	10.3	12.9	13.2	11.3	10.7	9.3	8.9	8.8	8.2	8.5	8.2	7.6	7.5	7.5	
Core 3: Inflation excl Energy and Utility Volatile Food Items & Transportation	9.1	13.3	13.3	10.5	10.3	9.3	8.9	8.1	7.6	7.8	7.5	7.0	6.8	6.9	
Core 4: Inflation excl All Food Items, Energy & Utility	3.1	5.8	9.1	7.4	7.3	8.5	8.3	7.5	7.5	7.4	6.5	6.1	5.9	5.7	
Bank of Ghana Urban Price Inflation	11.9	18.0	19.1	14.1	10.6	9.3	9.0	9.4	8.7	8.4	8.4	8.5	8.5	NA	