S&P Global Ratings

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Research Update:

Ghana Ratings Raised To 'B' On Improved Monetary Policy Effectiveness; Outlook Stable

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Overview

- Ghana's improving banking sector stability and lower inflation support our view that the effectiveness and transmission mechanism of its monetary policy have improved.
- We are therefore raising our long-term ratings on Ghana to 'B' from 'B-'. We are affirming the short-term foreign and local currency sovereign credit ratings at 'B'.
- The outlook is stable.

Rating Action

On Sept. 14, 2018, S&P Global Ratings raised its long-term foreign and local currency sovereign credit ratings on Ghana to 'B' from 'B-'. The outlook is stable. We affirmed the short-term foreign and local currency sovereign credit ratings at 'B'. At the same time, we revised our transfer and convertibility (T&C) assessment to 'B+' from 'B'.

The upgrade reflects our assessment that Ghana's monetary policy effectiveness has improved, albeit from a low base, and will support the credibility of the inflation-targeting framework over the period.

Outlook

The stable outlook balances Ghana's fairly robust growth prospects, decreasing inflation, and narrower current account deficits against risks from still-high budget deficits and a high stock of public sector debt.

We could lower our ratings if Ghana's economic growth is significantly lower than we expect and if its policymaking effectiveness were to weaken, for example if fiscal deficits were to be materially larger than our expectations.

We could consider raising our ratings if Ghana implements and adheres to measures that materially alleviate pressures on public finances and reduce public debt levels beyond our expectations. We could also see prospects for an upgrade if the current account deficit narrows faster than we expect and external debt and gross external financing needs are significantly reduced.

Rationale

The upgrade reflects our assessment that Ghana's monetary policy effectiveness has improved, albeit from a low base, and will support the credibility of the inflation-targeting framework over the period. Having peaked at a seven-year high of 19.2% (year-on-year) in March 2016, headline inflation has continued to decline to 10% by mid-year 2018, supported by a relatively tight monetary policy stance. In our view, the Bank of Ghana's (BoG) policy rate has also been fairly effectively transmitted through the financial system to market participants. The government's recapitalization of the banking system in 2018 is a fiscal expense weighing on our fiscal assessment, but should ultimately strengthen the banks and allow them to support financial intermediation in the economy.

The ratings are supported by our monetary policy assessment and our view of Ghana's fairly robust economic growth prospects. The ratings remain constrained by weak public finances from both a stock and flow perspective, sizable contingent liabilities, the country's low GDP per capita, and high external debt levels.

Institutional and Economic Profile: Stable political situation and robust growth prospects

- Ghana is one of Africa's most established democracies, with a track record of peaceful transitions of power spanning almost three decades.
- The government is attempting to establish a firm fiscal consolidation path while embarking on an ambitious economic reform program, which together could reduce key rating weaknesses.
- The economy is reasonably well diversified and economic growth is above that of peers.

We view Ghana as one of the most stable democracies in Africa. This was most recently illustrated by another smooth transition of power at the December 2016 elections to the New Patriotic Party (NPP), from the National Democratic Congress (NDC). Nevertheless, we think the frail state of public finances highlights institutional weakness, while transparency and policy predictability are limited.

The government started to more effectively address its weak public finances in 2017 and as a result we expect a modest reduction in general government deficits to an average of 5% of GDP over 2019-2021, from an average of 8% of GDP in the four years to 2017. We note that the government plans to introduce a legally binding cap to fiscal deficits, at 5% of GDP, subject to parliamentary approval. While we view these efforts positively, we think it will be challenging for the government to implement much-needed fiscal consolidation and establish a clear set of fiscal boundaries, while simultaneously attempting to introduce growth-enhancing economic reforms (albeit with substantial private sector input expected). The government's plan to build a new factory in each of Ghana's 275 districts is premised on private sector participation, with a limited amount of publicly financed seed capital, and therefore may not pose a significant fiscal burden.

Ghana's relatively stable political landscape remains an important factor in attracting external financing and overall levels of investment. Ghana's economy remains dominated by services (about 50% of GDP), with agriculture contributing a substantial 22% and the hydrocarbons sector contributing about 9%. The economy is therefore vulnerable to weather conditions and oil price fluctuations.

Since the discovery of oil in 2007 and Ghana's emergence as a viable oil producer in 2010, the hydrocarbon sector has become a significant sector of the economy. Over 2017, oil production increased significantly as two new fields came online, contributing 3.5 percentage points to real GDP growth of 8.5%. Non-oil economic activity also improved over the year, supported by an increase in cocoa and gold production by 25% and 20%, respectively.

We expect economic growth to slow down to about 5.4% in 2018, reflecting lower growth in oil production and a fall in cocoa output compared to 2017. Oil production is set to average around 175,000 barrels per day (b/d) in 2018, and the remedying of technical problems in the Jubilee field by year-end 2018 should push production to about 210,000 b/d by 2019. Agriculture growth will likely be restrained by unfavorable prospects for the cocoa sector owing partly to aging cocoa plants.

We project economic growth to ease to a still-robust 5% in the medium term. Our GDP per capita estimate is $1,800 in 2018, and we expect that the growth trend will remain somewhat above peers' with similar levels of GDP per capita. Our growth assumptions factor in broadly stable oil production at about 200,000 b/d and the expected dampening effects on economic activity of fiscal consolidation and relatively tight monetary policy. The development of the ancillary gas sector and the introduction of new generating facilities should alleviate the previous issues associated with electricity provision, and this could support manufacturing activity in the medium term.

Flexibility and Performance Profile: Monetary policy effectiveness has improved, but fiscal accounts remain weak

- Reduced inflationary pressures and broad alignment of money market interest rates with the BoG's policy rate indicate improved monetary policy effectiveness, in our view.
- Ghana's public finances remain weak from both a stock and flow perspective. The government has limited room to manoeuver. Both revenue mobilization and expenditure control are essential for the government to keep firmly on the consolidation path.
- We expect external debt to exceed external liquid assets by about 135% of current account receipts (CARs) on average over 2018-2021 and gross external financing needs to average about 120% of CARs plus usable

reserves.

The monetary transmission mechanism has strengthened, in our view, although we continue to view monetary policy credibility and effectiveness as a concern due to still-high consumer price inflation. The BoG's targeted rate of inflation is 8% plus or minus 2%.

The BoG reduced the policy interest rate from a peak of 26% in November 2015 to 17% in May 2018 on the back of improving macroeconomic conditions and falling inflation expectations. Recent developments in the money market have been broadly aligned within the monetary policy corridor of plus or minus 1%. In particular, the weighted average interbank rate declined to 16.4% in June 2018 from 24.9% in November 2015. Although commercial lending rates remain high due to credit risk, they have also declined by more than 500 basis points since early 2017.

In our view, credit risk within the banking sector remains high, reflected by improving, but still-high levels of nonperforming loans (NPLs), at about 23% of total loans in June 2018.

The government's Energy Sector Levy Act (ESLA) could help resolve some of the bank asset quality issues. Bank lending to energy sector state-owned enterprises (SOEs) accounts for a large part of banking system NPLs. Under the ESLA Bond Program, a special-purpose vehicle (SPV) will enter into agreements with relevant SOEs' creditors, under which the legacy debts will either be repaid in cash from the proceeds of the bond issuances, or be settled through debt-swap transactions. In swap transactions, the legacy debt will be traded directly for bonds issued under the program.

We think that the ESLA bonds could help improve bank asset quality, put bank balance sheets in a stronger position, facilitate private credit growth, and further strengthen the effectiveness of monetary policy transmission. More-effective open market operations and the development of financial system and domestic bond market should also be supported by the government's strategy of refinancing short-term debt with longer-dated bonds (especially five-year, seven-year, and 10-year bonds) in the domestic bond market over the past year, and in the near future will extend the yield curve.

In pursuit of strengthening the banking sector and ensuring financial stability, in August 2017, the BoG approved the acquisition of two banks by GCB Bank. Subsequently, in April 2018, the Ministry of Finance issued a Ghanaian cedi (GHS) 2.2 billion bond in order to close the asset-liability mismatch. In August 2018, the BoG merged another five banks into one, with the government injecting GHS450 million in capital while also issuing another GHS5.76 billion bond to bridge the asset-liability gap. We estimate the fiscal costs of these bailouts at 3.5% of GDP and take into account in our projections of fiscal deficit and government indebtedness.

The BoG has also increased the minimum capital requirement for all banks to

GHS400 million from GHS120 million. We expect that increased statuary capital will flow into the banking sector from private shareholders by December 2018 and provide additional capital buffers to support private sector lending in the medium term.

We estimate the general government deficit at 8% of GDP in 2018 when we include the costs of the bank bailout. Excluding the banking system bailout, we estimate the 2018 fiscal deficit at 4.5% of GDP, in line with the official budget forecast, which improved from 6% in 2017 and 10.2% in 2016. The change in net general government debt is estimated at 10.5% in 2018 and will average 7.6% per year in 2018-2021.

Ghana achieved some fiscal consolidation in 2017. Although the 2017 revenue performance was marked by a large shortfall in relation to the budget, expenditures were pared back in response. In particular, grants to other government units, including transfers to statutory funds, were contained and the clearance of arrears was lower than budgeted.

In 2018, we note that new tax administration and compliance measures will not come into effect until the third quarter of the year. As a result, we expect the authorities to rely on further expenditure constraints to meet their fiscal deficit target for 2018. Through 2021, we expect government budget deficits, absent one-offs, to remain around 5.0% of GDP. Our projections rest on assumptions that the authorities will strengthen revenue administration and broaden the tax base, as non-discretionary spending on wages and interest payments already absorb more than 90% of current total tax revenues. The run-up to the election year of 2020 might see faster spending growth. We also expect that capital spending will remain quite robust because Ghana still has sizable infrastructure deficiencies, despite some successes, including an upgraded network of key roads and wider public access to electricity and water.

We estimate Ghana's net government debt position (net of liquid assets) at 65% of GDP in 2018 and expect a gradual reduction to 60% by 2021, with interest costs continuing to consume around 30% of government revenues each year.

Due to the refinancing of government short-term local currency debt with longer-dated bonds, short-term debt reduced to 8.5% of total government debt in 2017 from 16.5% in 2016. At the same time, interest rates for 91-day treasury bills have started to reduce to about 13% in December 2017 from 16.81% in December 2016, and there is a similar trend for all other maturities. At end-2017, 71% of total government debt was external, with 53% denominated in foreign currency. As a result, the debt stock is sensitive to the cedi's depreciation.

Non-resident holdings of government local currency debt have increased to 38% in 2017 from about 22% in 2016. With the exchange rate relatively stable and inflation reducing recently, high real returns on local currency debt have been attractive to foreign investors. Although ongoing fiscal and banking sector reforms will underpin rising investor confidence, there remains a risk of capital outflows given the recent surge in portfolio inflows into local government debt.

The size of energy sector SOE debt, much of which is overdue, has been estimated at about 13% of GDP, which we assess as a moderate contingent liability for the government. The government's ESLA bond program is expected to be worth about 5% of GDP when fully drawn (currently issued debt is around 2.5% of GDP) and will replace existing SOE debt. It is therefore not an additional contingent liability of the government, in our view. Energy sector SOEs, in particular the Volta River Authority and Electricity Company of Ghana, have experienced substantial losses, despite increased tariffs in the previous years. A reduction in utility tariffs in 2018 could pose additional financial challenges to the utility SOEs if an expected increase in demand does not materialize or greater use of cheaper domestic gas does not yield expected cost efficiency.

Ghana's current account balance has improved significantly in recent years due to increased commodity exports, with a deficit of 12% in 2013 shrinking to about 4.2% in 2017. We expect the current account deficit to narrow to about 3% by 2021. We expect oil production to reach an all-time high of about 210,000 b/d in 2019 and remain broadly stable through 2021. We expect narrowing deficits will also be supported by relatively strong cocoa prices and a reduction in refined petroleum and gas imports, as the Sankofa field commenced significant gas production in the second half of 2018. We expect gross foreign exchange reserves to rise to US$7.5 billion by 2021 and remain at around 3.5 months of import coverage.

Key Statistics

Table 1

Ghana Selected Indicators

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
ECONOMIC INDICATORS (%)										
Nominal GDP (bil. GHS)	75	93	113	137	167	206	241	281	320	364
Nominal GDP (bil. $)	42	48	39	37	43	47	52	57	62	67
GDP per capita ($000s)	1.6	1.8	1.4	1.4	1.5	1.6	1.8	1.9	2.0	2.1
Real GDP growth	9.3	7.3	4.0	3.8	3.7	8.5	5.4	5.9	4.5	4.5
Real GDP per capita growth	6.7	4.8	1.6	1.5	1.4	6.1	3.1	3.6	2.2	2.2
Real investment growth	42.4	(26.1)	19.7	6.6	(12.0)	0.9	4.0	4.0	3.5	4.5
Investment/GDP	17.0	13.3	18.8	16.7	14.5	12.2	11.1	10.1	9.5	9.0
Savings/GDP	5.3	1.3	9.4	9.1	7.8	8.0	6.1	6.1	6.4	5.8
Exports/GDP	40.4	34.2	39.5	45.5	41.0	43.9	41.0	38.5	36.7	34.2
Real exports growth	15.2	(3.6)	(5.8)	8.1	5.9	16.5	3.0	5.0	4.5	2.0
Unemployment rate	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2
EXTERNAL INDICATORS (%)										
Current account balance/GDP	(11.7)	(11.9)	(9.5)	(7.6)	(6.6)	(4.2)	(5.0)	(4.0)	(3.1)	(3.2)

Table 1

Ghana Selected Indicators (cont.)										
Current account balance/CARs	(25.5)	(31.0)	(21.3)	(14.5)	(14.8)	(8.7)	(10.9)	(9.4)	(7.6)	(8.6)
CARs/GDP	46.0	38.6	44.5	52.1	44.8	49.0	45.7	42.8	40.7	37.9
Trade balance/GDP	(10.0)	(8.0)	(3.5)	(8.4)	(4.2)	2.5	2.2	2.3	2.3	1.7
Net FDI/GDP	7.9	6.7	8.6	8.0	8.1	6.8	6.0	6.0	5.5	5.0
Net portfolio equity inflow/GDP	(0.3)	(0.6)	(0.4)	(0.6)	(0.6)	(0.8)	(0.7)	(0.7)	(0.7)	(0.7)
Gross external financing needs/CARs plus usable reserves	113.8	118.9	119.4	119.0	125.0	118.1	122.1	124.7	121.8	120.0
Narrow net external debt/CARs	65.5	100.1	118.4	128.1	135.2	125.8	130.5	133.7	134.6	140.0
Narrow net external debt/CAPs	52.2	76.4	97.7	111.8	117.7	115.8	117.6	122.2	125.0	129.0
Net external liabilities/CARs	137.1	183.3	229.4	237.6	262.7	241.9	250.2	259.5	264.5	276.2
Net external liabilities/CAPs	109.2	140.0	189.2	207.5	228.8	222.6	225.5	237.3	245.8	254.4
Short-term external debt by remaining maturity/CARs	20.1	22.4	33.8	31.1	38.9	34.2	39.2	42.8	42.9	43.9
Usable reserves/CAPs (months)	2.7	2.7	3.0	2.3	2.4	2.3	2.5	2.4	2.6	3.0
Usable reserves (mil. $)	5,349	5,188	4,349	4,403	4,862	5,491	5,384	5,947	6,870	7,508
FISCAL INDICATORS (%, general government)										
Balance/GDP	(10.3)	(11.1)	(10.1)	(7.0)	(10.2)	(6.0)	(8.0)	(5.0)	(5.0)	(4.0)
Change in net debt/GDP	17.3	17.6	19.6	15.4	11.5	8.7	10.5	7.0	7.0	6.0
Primary balance/GDP	(7.1)	(6.4)	(3.9)	(0.4)	(3.3)	0.6	(1.8)	1.0	0.9	1.5
Revenue/GDP	22.1	19.9	20.8	21.9	19.1	19.2	19.5	19.5	20.0	20.0
Expenditures/GDP	32.4	31.0	30.9	28.9	29.3	25.2	27.5	24.5	25.0	24.0
Interest /revenues	14.6	23.6	30.1	30.3	36.0	34.3	31.9	30.8	29.5	27.6
Debt/GDP	47.8	57.6	69.9	73.1	73.4	69.2	70.2	67.3	66.1	64.0
Debt/Revenue	216.0	288.9	336.7	334.2	383.2	360.6	360.2	345.9	331.4	320.7
Net debt/GDP	45.9	54.6	64.7	68.9	67.9	63.9	65.1	62.9	62.2	60.6
Liquid assets/GDP	1.9	3.0	5.2	4.3	5.5	5.4	5.1	4.6	4.1	3.5
MONETARY INDICATORS (%)										
CPI growth	9.2	11.7	15.5	17.2	17.5	12.4	10.0	9.0	9.0	8.0
GDP deflator growth	15.2	15.6	16.7	16.4	17.8	13.4	11.0	10.0	9.0	9.0
Exchange rate, year-end (GHS/$)	1.88	2.20	3.20	3.79	4.20	4.42	4.80	5.04	5.29	5.56
Banks' claims on resident non-gov't sector growth	29.0	31.9	42.4	29.0	13.0	19.4	5.0	10.0	15.0	15.0
Banks' claims on resident non-gov't sector/GDP	15.9	16.9	19.9	21.2	19.6	19.1	17.1	16.2	16.3	16.5
Foreign currency share of claims by banks on residents	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Foreign currency share of residents' bank deposits	28.9	29.1	31.1	30.6	28.4	25.4	22.6	23.9	25.2	26.6
Real effective exchange rate growth	(8.0)	0.7	(22.4)	1.5	14.0	(1.7)	N/A	N/A	N/A	N/A

Table 1

Ghana Selected Indicators (cont.)
Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid assets held by nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. GHS--Ghanaian cedi. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. The data and ratios above result from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Table 2

Ghana Ratings Score Snapshot

Key rating factors	
Institutional assessment	5
Economic assessment	4
External assessment	6
Fiscal assessment: flexibility and performance	6
Fiscal assessment: debt burden	6
Monetary assessment	4

S&P Global Ratings' analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Sovereign Rating Methodology," published on Dec. 18, 2017, details how we derive and combine the scores and then derive the sovereign foreign currency rating. In accordance with S&P Global Ratings' sovereign ratings methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating the committee can make use of the flexibility afforded by §15 and §§126-128 of the rating methodology.

Related Criteria

- Criteria - Governments - Sovereigns: Sovereign Rating Methodology, Dec. 18, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Sovereign Ratings History, Sept. 5, 2018
- Sovereign Ratings List, Sept. 5, 2018
- Sovereign Debt 2018: Global Borrowing To Remain Steady At US$7.4 Trillion,

Feb. 22, 2018

- Sovereign Debt 2018: Sub-Saharan Africa Borrowing To Rise To US$57 Billion , Feb. 22, 2018
- Global Sovereign Rating Trends Midyear 2018, July 16, 2018
- Sub-Saharan Africa Sovereign Rating Trends Midyear 2018, July 16, 2018
- Sovereign Risk Indicators, July 5, 2018. An interactive version is available at www.spratings.com/sri
- 2016 Sovereign Ratings Update: Outlook And CreditWatch Resolutions, April 18, 2017
- Default, Transition, and Recovery: 2016 Annual Sovereign Default Study And Rating Transitions, April 3, 2017

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision. After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Upgraded; Ratings Affirmed

	To	From
Ghana		
Sovereign Credit Rating	B/Stable/B	B-/Positive/B
Transfer & Convertibility Assessment	B+	B
Senior Unsecured	B	B-

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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.