



# Bank of Ghana Monetary Policy Report

## Inflation Outlook and Analysis

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### 1.0 Overview of Global and Domestic Economic Developments

Global growth momentum has remained firm, following from the Covid-19 shock, largely reflecting continued policy support, mass vaccinations, and removal of restrictions across several advanced countries. Notwithstanding the progress made, recent developments associated with the rapid spread of new Covid-19 variants, vaccine hesitancy in some advanced economies and lack of vaccine availability across emerging market and developing economies, have heightened uncertainties and could potentially undermine the broad-based recovery of the global economy.

Global financing conditions have tightened somewhat as prospects of strong growth and higher inflation expectations pushed up borrowing costs in advanced economies. However, the continued accommodative monetary policy stance by major central banks has moderated sovereign and corporate bond spreads and so far, contained capital flow reversals, as well as supported the rebound in equity markets and higher portfolio flows to emerging market economies. In broad terms, financing conditions remain favourable and supportive of the recovery process.

Headline inflation in several advanced and emerging market economies have picked up sharply above targets since the beginning of 2021, driven mainly by base-drift effect, energy price pressures, and supply constraints amidst increased consumer demand as economies re-open. However, the expectation for headline inflation to return to target over the medium-term, moderated by the still sizeable spare capacity, slack in labour market conditions and restrained wage growth. In emerging market and frontier economies, the pace of price movements would be dictated by currency movements and Covid-related supply-side constraints.

The domestic economy continues to recover after the sharp moderation in the growth momentum at the instance of the COVID-19 pandemic. The Ghana Statistical Service reported an estimated GDP growth of 3.1 percent for the first quarter of 2021, lower than the pre-pandemic growth of 7.0 percent recorded for the first quarter of 2020. Non-oil GDP grew by 4.6 percent, from 7.9 percent growth in the same comparative period.

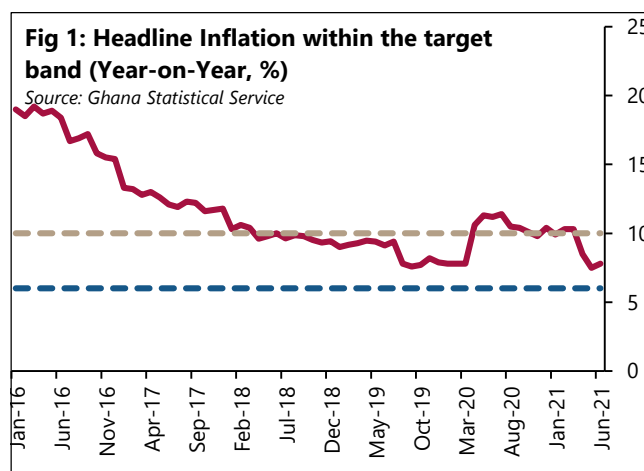
Beyond the first quarter GDP outturn, high frequency economic indicators for the second quarter of the year point to a sharp pickup in economic activity relative to last year. The Bank’s updated Composite Index of Economic Activity (CIEA) recorded a strong annual growth of 33.1 percent in May 2021, relative to the contraction of 10.2 percent recorded in the corresponding period in 2020. The sharp increase broadly reflects vaccine rollout efforts, some base-drift effects as well as improvement in industrial production activities, domestic consumption, pick up in import activities, steady rise in construction activities and a rise in air-passenger arrivals, during the period.

The latest confidence surveys by the Bank of Ghana showed mixed outturns. Consumer sentiments softened on the back of a variety of factors including the implementation of the recently announced revenue measures contained in the 2021 Budget, while business sentiments remained somewhat broadly unchanged due to expectations of improvement in company growth prospects.

## 2.0 Domestic Price Developments

### Headline Inflation

Domestic price pressures moderated during the second quarter of 2021. Headline inflation declined significantly from 10.3 percent in March 2021 to 7.5 percent in May 2021, before ticking up to 7.8 percent in June 2021. This trend has pushed inflation below the central path of the medium-term target band. The downward trajectory of inflation was largely driven by the tight monetary policy stance and some base drift effects, which reflected in both food and non-food prices. Food inflation dipped markedly from 10.8 percent in March to 6.5 percent in April, to 5.4 percent in May 2021 and then up to 7.3 percent in June 2021. Non-food inflation on the other hand has declined



persistently, falling from 10.0 percent in March to 8.2 percent in June 2021.

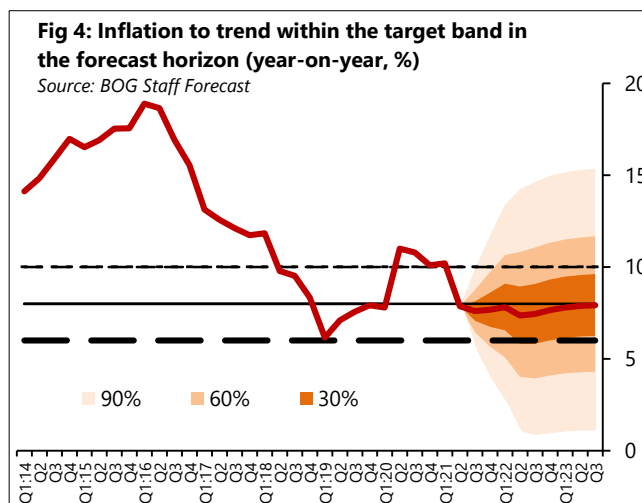
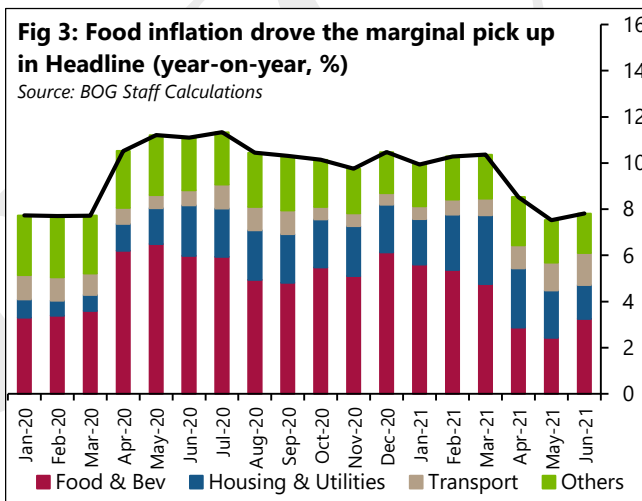
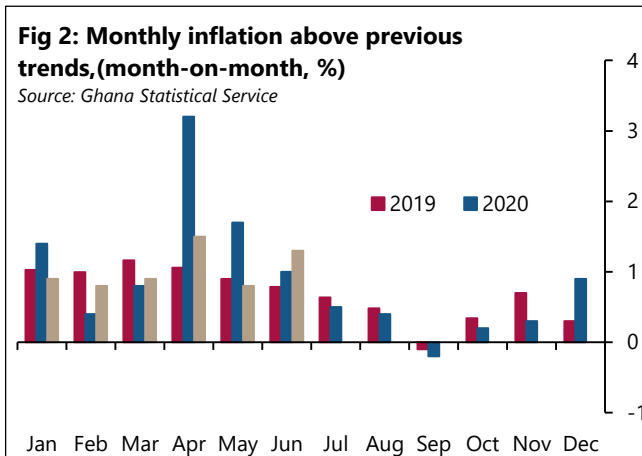
In line with these trends, underlying inflationary pressures broadly eased across all the Bank's core measures of inflation over the same period. The core inflation measure which excludes energy and utility, declined from 10.9 percent in March 2021 to 8.6 percent in April, 7.3 percent in May, before ticking up slightly to 7.5 percent in June. The overall weighted inflation expectations index declined in June 2021, on account of lower businesses and financial sector inflation expectations, despite the slight pick-up in consumer inflation expectations.

Month-on-month inflation fell to 0.8 percent in May 2021 from 1.5 percent in April and climbed to 1.3 percent in June. Monthly food inflation declined to 1.3 percent in May from 2.3 percent in April 2021 and picked up to 1.8 percent in June.

Similarly, non-food monthly inflation dropped to 0.4 percent in May from 1.0 percent in April and doubled to 0.8 percent in June 2021. The rise in both food and non-food prices in June partly reflected the adjustment in transport fares. In terms of drivers of year-on-year inflation, food pressures eased from April to May before inching up in June. Non-food price pressures have continued to ease over the period. The marginal pick up in food inflation in June came mainly on the back of fruit-bearing vegetables, ready-made food, and cereals. The ease in non-food inflation over the period was broad based.

### 3.0 Inflation outlook

Inflation is projected to remain below the central path in the medium-term, barring any unforeseen



shocks. This reflects favourable base-drift effects due to the waning impact of Covid-induced spike in food prices which occurred in the second quarter of 2020 and tight monetary policy stance in the outlook. In the baseline forecast, food and non-food inflation are projected to hover around the central path, driven broadly by low production costs. Imported inflation is expected to exert some upward pressures as prices continue to remain elevated in the US.

Costs in both the food and non-food sectors are projected to be low, reflecting the prevailing spare capacity (negative output gap), as well as the projected stability of the exchange rate in the outlook. However, production costs are projected to rise in the medium-term as economic activity fully recover. Real sector activity is projected to remain below potential in the near-term, on the back of tighter monetary conditions, real sector expectations, and fiscal consolidation. Economic activity is expected to approach full capacity in the medium-term driven by higher impulses from global demand and improvement in expectations of economic agents as the economy better adapts to the Covid-19 pandemic.

### **3.1 Risks to the Inflation outlook**

Assessment of risks to the inflation outlook from global economic conditions, domestic economic activity, and government's fiscal policy implementation amid the pandemic suggests that the balance of risks to the inflation outlook are largely muted. The key risks as assessed include:

- ***Global Inflation***

Global inflation continues to surge in most advanced economies, driven by elevated crude oil prices, base-drift effects and temporary supply-demand imbalances as supply bottlenecks reflect in changing consumer spending patterns. The firming up of inflation expectations across the globe is expected to exert pressure on domestic inflation through the imported price channel in the near-term. Various measures of underlying inflation, however, remain subdued due to sizeable spare capacity and the significant slack in labour markets. Food price pressures and pass-through of higher oil prices are expected to keep inflation elevated in some emerging market and developing economies. Although uncertainty about global inflation dynamics remains high, global inflation is projected to ease as pandemic-related disruptions and supply-demand mismatches wane in the outlook. Continued stability of the exchange rate would limit the pass-through of imported inflation and help anchor domestic prices in the outlook.

- ***Domestic economic activity***

High frequency data for the second quarter of the year point to a sharp pickup in activity relative to last year. The Bank's updated Composite Index of Economic Activity (CIEA) rebounded strongly recording an annual growth of 33.1 percent in May 2021, compared to a contraction of 10.2 percent same time last year.

Similarly, the latest Ghana Purchasers Managers Index, which gauges the rate of inventory accumulation by managers of private sector firms and measures dynamics in economic activity, indicated some sustained levels of activity.

- ***Domestic food price pressures***

Despite the sharp decline in food inflation in recent months, pressures on food prices are emerging. The recent outbreak of bird flu disease which has restricted the movements of poultry and poultry products within and from affected regions could drive up the prices of poultry products. Also, changes in the weather pattern could significantly lower food production and put upward pressures on food prices in the outlook.

- ***Fiscal pressures***

On fiscal operations, the budget deficit exceeded its target in the first five months mainly on the back of revenue underperformance. Going forward, expenditure has to be aligned to revenue performance to support the fiscal consolidation efforts. The recent level of public debt raises debt sustainability concerns hence the importance and urgency of fiscal consolidation efforts. Greater efficiency in debt management would be required, especially in the face of potential further tightening of global financing conditions which could heighten rollover risks and access to new financing in the outlook. This calls for vigilance and complementarity in fiscal and monetary policies to signal strong commitment to the consolidation process.

- ***Rising Ex-pump Prices***

Rising international crude oil prices and its attendant upward adjustment in ex-pump prices would exert some inflationary pressures in the outlook. The recent upward adjustment of transport fares is likely to lead to second-round pricing effects on most items in the CPI basket since transport costs form part of the price components of most products. However, if crude oil prices stabilize at its current levels, the impact of ex-pump prices on headline inflation in the outlook would be muted since the direct impact of the current crude oil price has already reflected in the CPI.

#### **4.0 Conclusion**

Headline inflation fell to 7.8 percent in June 2021 lower than the central path of 8.0 percent of the medium-term target band for the first time since March 2020. The decline in inflation was consistent with the forecast presented at the May MPC Meeting. The July baseline projection forecasts inflation to remain within the medium-term target band of  $8 \pm 2$  percent in the outlook barring any unforeseen shocks, especially fiscal slippages. The key upside risks to the outlook include the projected uptick in food prices, rising ex-pump prices of petroleum products and possible fiscal pressures in the outlook.

**Appendix Table 1: CPI Components**

	Headline Inflation (%)			Monthly Changes in CPI (%)		
	Combined	Food	Non-food	Combined	Food	Non-food
<b>Dec-18</b>	<b>9.4</b>	<b>8.7</b>	<b>9.8</b>	<b>1.1</b>	<b>1.3</b>	<b>1.0</b>
<b>Dec-19</b>	<b>7.9</b>	<b>7.2</b>	<b>8.5</b>	<b>0.3</b>	<b>-0.6</b>	<b>1.0</b>
<b>2020</b>						
Jan	7.8	7.8	7.9	1.4	2.3	0.8
Feb	7.8	7.9	7.7	0.4	0.5	0.4
Mar	7.8	8.4	7.4	0.8	1.6	0.3
Apr	10.6	14.4	7.7	3.2	6.4	0.8
May	11.3	15.1	8.4	1.7	2.3	1.3
Jun	11.2	13.8	9.2	1.0	0.1	1.8
Jul	11.4	13.7	9.7	0.5	0.0	0.9
Aug	10.5	11.4	9.9	-0.4	-1.1	0.2
Sept	10.4	11.2	9.8	-0.2	-0.5	0.1
Oct	10.1	12.6	8.3	0.2	0.1	0.3
Nov	9.8	11.7	8.3	0.3	0.3	0.3
Dec	10.4	14.1	7.7	0.9	1.5	0.4
<b>2021</b>						
Jan	9.9	12.8	7.7	0.9	1.2	0.7
Feb	10.3	12.3	8.8	0.8	0.0	1.4
Mar	10.3	10.8	10.0	0.9	0.2	1.4
Apr	8.5	6.5	10.2	1.5	2.3	1.0
May	7.5	5.4	9.2	0.8	1.3	0.4
Jun	7.8	7.3	8.2	1.3	1.8	0.8

Source: Ghana Statistical Service

**Appendix Table 2: Headline Inflation**

CPI Components (%)													
	Weights (%)	2020						2021					
		Mar	Apr	May	Jun	Sept	Dec	Jan	Feb	Mar	Apr	May	Jun
<b>Overall</b>	100.0	7.8	10.6	11.3	11.2	10.4	10.4	9.9	10.3	10.3	8.5	7.5	7.8
<b>Food and Beverages</b>	43.1	8.4	14.4	15.1	13.8	11.2	14.1	12.8	12.3	10.8	6.5	5.4	7.3
<b>Non-food</b>	56.9	7.4	7.7	8.4	9.2	9.8	7.7	7.7	8.8	10.0	10.2	9.2	8.2
Alcoholic Beverages, Tobacco	3.7	11.4	9.7	10.1	8.6	9.0	6.0	7.4	7.2	7.0	8.0	7.3	6.5
Clothing and footwear	8.1	8.4	8.3	7.9	7.3	8.0	7.9	7.2	6.2	6.0	7.1	6.5	6.0
Housing and Utilities	10.2	6.7	11.2	15.1	21.3	20.3	20.1	19.0	23.4	29.0	25.0	19.9	14.2
Furnish, H/H Equipt. Etc	3.2	4.3	4.6	4.5	4.9	4.9	4.7	4.5	5.0	4.7	4.9	4.6	4.7
Health	0.7	6.2	6.5	5.6	7.8	8.9	6.0	6.9	6.9	7.1	7.4	8.4	6.0
Transport	10.1	9.2	6.7	5.4	6.3	10.1	4.8	5.4	6.2	6.8	9.6	11.7	13.4
Information and Communication	3.6	3.0	4.0	6.2	6.3	6.8	7.0	6.7	8.4	8.1	7.4	5.1	4.9
Recreation & Culture	3.5	9.0	8.6	9.4	5.8	3.4	1.8	3.0	3.9	4.0	5.1	3.6	3.6
Education	6.5	6.8	6.9	7.1	4.1	4.2	0.2	0.3	0.4	0.4	0.6	0.8	0.9
Restaurants and Accommodation	4.6	3.5	3.6	4.3	5.8	7.0	5.4	4.8	5.4	6.1	6.7	6.0	4.8
Insurance and Financial services	0.2	0.1	0.1	0.2	3.5	2.0	3.3	3.3	7.4	7.8	9.0	9.0	5.5
Miscellaneous goods & services	2.4	7.3	6.4	5.9	5.4	4.6	3.8	5.1	4.3	4.5	5.2	4.4	4.5

Source: Ghana Statistical Service