



ECON 216

Economy of Ghana II

Session 3 – Inflation in Ghana I : Definition and Trends

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Session Overview

- ❑ In the preceding session we discussed the conduct of monetary policy in Ghana and the functions Central Bank (Bank of Ghana).
- ❑ Price stability or inflation control is the core responsibility of Bank of Ghana.
- ❑ Thus, the Central Bank through measures and interventions it deems necessary and appropriate ensures price stability.
- ❑ This session assess trends and analyses the performance of Bank of Ghana in controlling inflation over the years.
- ❑ This session will introduce students to inflation in Ghana, emphasising the definition, trends and analysis of inflation in Ghana.

Session Overview

- ❑ At the end of this session, students should be able to:
 - ❖ Comprehend the meaning of inflation and differentiate between inflation, deflation and disinflation.
 - ❖ Discuss inflationary trends in Ghana over the years.
 - ❖ Explain the various methods used in estimating inflation in the Ghanaian economy.
 - ❖ Appreciate Ghana's recent inflation experience

Session Outline

- ❑ The key topics to be covered in the session are as follows:
 - ❖ Topic One : Definition of Inflation
 - ❖ Topic Two : Measurement of Inflation in Ghana
 - ❖ Topic Three: Trends of Inflation in Ghana
 - ❖ Topic Four : Ghana's Recent Inflation Experience

Reading List

- ❑ Institute of Statistical, Social and Economic Research (Various Editions). The State of the Ghanaian Economy.
- ❑ Quartey, P., & Afful-Mensah, G. (2014). Financial and monetary policies in Ghana: A review of recent trends. *Review of Development Finance*, 4(2), 115-125.
- ❑ <http://www.sciencedirect.com/science/article/pii/S1879933714000189>
- ❑ Osei, V. (2015). Inflation Dynamics in Ghana. *International Finance and Banking*, 2(1), 38.
- ❑ <http://www.macrothink.org/journal/index.php/ifb/article/view/7913>

Topic One

DEFINITION OF INFLATION

What is Inflation?

- ❑ Inflation or more appropriately, the rate of inflation (inflation rate), is a measure of the rate at which average prices change in an economy over a period time.
- ❑ More specifically, the rate of inflation measures the rate at which the average price level increases over a period time, usually a year.
- ❑ Consequently, inflation may be simply defined as a sustained and persistent increase in the general price level.
- ❑ The inflation rate indicates or reports the rate at which these increases occur over a period of time, say a year.

What is Inflation?

- ❑ A decrease in the inflation rate from 10% to 5% does not mean the average prices have declined. It only means the rate at which the average prices are rising have reduced from 10% to 5%.
- ❑ Also, inflation does not imply high prices. It only means prices are rising at some rate.
- ❑ Another point worth noting is that the inflation rate is computed using the notion of the average price level. This average is based on a basket of goods and services consumed by representative households in the economy.

What is Inflation?

- ❑ Hence, not all goods and services are included in this basket.
- ❑ Consequently, the effects of changes in prices will affect different households, differently.
- ❑ Thus, there could be a dichotomy between the statistical measurement of inflation and the cost of living.
- ❑ Note that the opposite of inflation is deflation, where we observe a sustained decrease in the price level over time.

Topic Two

MEASUREMENT OF INFLATION IN GHANA

Measurement of Inflation

- ❑ The common measure of the rate of inflation is the rate of change of the Consumer Price Index (CPI).
- ❑ The Consumer Price Index (CPI) measures the weighted average of cost of a basket of goods and services that households acquire for the purpose of consumption.
- ❑ In Ghana, the responsibility of estimating inflation lies with the Ghana Statistical Service. They publish inflation rates on a regular basis – usually monthly.
- ❑ In calculating the CPI, the GSS determines a based year and currently it uses 2012 as the base year, with an index of 100. The GSS applies weight to the individual items in the basket.

Measurement of Inflation

- ❑ The major components for the computation have been divided into **Food (and Non-Alcoholic Beverages)** and Non-Food items. This distinction allows for a better understanding of the inflationary pressures within the economy.
- ❑ Food and Non-Alcoholic Beverages include: Vegetables including potatoes and other tuber vegetables; Bread and cereals; Fish; Fruit; Meat; Milk, cheese and eggs; Oils and fats; Food products; Sugar, jam, honey, syrups, chocolate and confectionery; Mineral waters, soft drinks and juices; Coffee, tea and cocoa.

Measurement of Inflation

- Non-Food include: Hotels, cafés and restaurants; Clothing and footwear; Furnishings, household equip. etc; Health; Transport; Housing, water, electricity, others; Recreation and culture; Alcoholic beverages etc; Miscellaneous; Education; Communications.
- Table 1 shows some selected weights assigned to some selected goods and services in the basket used in calculating the CPI.

Measurement of Inflation

Table 1: Selected items and weights

| ITEM | WEIGHT |
|--|--------|
| Food and non-alcoholic beverage | 43.9 |
| Communication | 2.7 |
| Health | 2.4 |
| Hotels, cafes and restaurants | 6.1 |
| Alcoholic beverages, tobacco and narcotics | 1.7 |
| Miscellaneous goods and services | 7.1 |
| Housing, water, electricity, gas and other fuels | 8.6 |
| Furnishing, household equipment and maintenance | 4.7 |
| Clothing and footwear | 9.0 |
| Transport | 7.3 |
| Education | 3.9 |
| Recreation and culture | 2.6 |

Measurement of Inflation in Ghana

Table 2: Consumer Price index, July 2015 – May 2016

| Year/Month | Index 2012 = 100 | Change rate (%) | |
|------------------|------------------|-----------------|--------------|
| | | Monthly (m/m) | Yearly (y/y) |
| July - 2015 | 154.5 | 2.3 | 17.9 |
| August - 2015 | 153.3 | -0.7 | 17.3 |
| September – 2015 | 153.1 | -0.1 | 17.4 |
| October – 2015 | 157.2 | 2.7 | 17.4 |
| November – 2015 | 158.9 | 1.0 | 17.6 |
| December – 2015 | 160.6 | 1.1 | 17.7 |
| January – 2016 | 168.2 | 4.6 | 19.0 |
| February – 2016 | 169.2 | 0.8 | 18.5 |
| March – 2016 | 172.0 | 1.7 | 19.2 |
| April – 2016 | 174.4 | 1.4 | 18.7 |
| May – 2016 | 176.4 | 1.1 | 18.9 |

Topic Three

TRENDS OF INFLATION IN GHANA

Trends of Inflation in Ghana

- ❑ Inflationary trends in Ghana may be divided into two periods: The Pre-ERP period (unto 1983) and the The Post-ERP period.
- ❑ In the immediate years after independence the country encountered very little inflationary pressures.
- ❑ But from 1964 when the country began to encounter balance of payments problems, inflationary pressures began to build up in Ghana.
- ❑ But since 1970 inflation has continued to present itself as a major economic problem in Ghana

Trends of Inflation in Ghana

- ❑ The Pre ERP era was characterised by massive government investments in import substitution industries and other investments on infrastructure and social facilities.
- ❑ This was shown in demand pressure than output expansion. This exerted strong pressure on prices.
- ❑ Inflation was mitigated through the use of external reserves to finance fiscal deficits and maintain import supplies.
- ❑ But as the reserves diminished and increased import duties failed to close the budget gap, the government had to resort to bank financing.

Trends of Inflation in Ghana

- ❑ Another factor that helped to sustain the pressure on prices was the increasingly challenge of foreign exchange constraint which led to shortages of most consumer items.
- ❑ Inflation was contained between 1969-71 through the increase in domestic production and tight monetary policies.
- ❑ The decade 1972-82 saw expansionary fiscal and monetary policies leading to widening budget deficits. Extensive controls of prices, the exchange rate, and interest rates, were used to contain the resulting inflationary pressures.

Trends of Inflation in Ghana

- ❑ Inflation averaged as high as 50% per annum during 1972-82/with 1977 and 1981 recording the highest-ever rates of 117% each.
- ❑ Clearly, inflation during the period 1972-82, reflected excessive demand pressure sustained by fiscal expansion and consequent monetary growth.
- ❑ The problem was made worse by inadequate growth of output and supplies due to particular structural constraints faced by the economy, particularly declining food production and manufacturing.

Trends of Inflation in Ghana

- ❑ The Government with the support of the World Bank and IMF adopted the Economic Recovery Program in mid-1983.
- ❑ The main objective of the programme was to stem the slide of the economy and establish a path to sustainable growth.
- ❑ The measures implemented included exchange rate corrections, price de-regulation, trade liberalization, financial management reforms and the rehabilitation of economic and social infrastructure.

Trends of Inflation in Ghana

- ❑ Inflation control under the ERP focused on reducing budget deficits and bank financing, as well as improving tax administration and expansion of the tax base.
- ❑ After the deregulation under the ERP, cost pressures have become an important factor in influencing inflation.
- ❑ Among these are pressures emanating from rising energy and utility prices and exchange rate depreciation.
- ❑ Thus, the sources of inflation in Ghana cannot be limited only to demand factors, but supply factors must also be taken into account

Topic Four

GHANA'S RECENT INFLATION EXPERIENCE

Ghana's Recent Inflation Experience

- ❑ Let us now look at **inflationary trends in recent times.**
- ❑ In recent years however, the country has not experienced the episodes of high inflation experienced throughout the mid-1970s to the end of the 1990s.
- ❑ There is now a generally accepted view/consensus that macroeconomic stability is essential in the process of economic growth and development.
- ❑ Thus, several government administrations have pursued policies aimed at ensuring macro-stability by stabilizing general price levels.



Ghana's Recent Inflation Experience

- **Insert Graph Here**



Ghana's Recent Inflation Experience

- ❑ Consequently, both the Bank of Ghana and the Ministry of Finance, and other related state MDAs as well as other public policy NGOs have continually spoken of the need to maintain macroeconomic stability.
- ❑ Improved policy measures, such as the setting up of the Monetary Policy Committee (MPC) of the Bank of Ghana and the pursuance of a single-digit inflation targeting regime appear to have helped in this regard.

Ghana's Recent Inflation Experience

- ❑ In spite of the recent successes at controlling inflation, there exist threats of inflation.
- ❑ Currency depreciation as a result of expansionary monetary policies and shortfalls in foreign exchange.
- ❑ Financial intermediation and depth remain low; weakening the transmission of monetary policy through interest rates.

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- Bawumia (2010): Monetary policy and financial sector reform in Africa: Ghana's experience.
- Kwakye J. K. (2013): Five years of inflation-targeting in Ghana: what has changed and what needs to change further to enhance the process? (www.ieagh.org/wp-content/uploads/2014/06/la-v20-n1.pdf)
- Kwakye, J. K. (2012). *Key issues in the choice of an appropriate monetary policy framework for Ghana.* (www.ieagh.org/wp-content/uploads/2014/07/mono-32.pdf)