IEA wants medium-term inflation target lowered

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The Institute for Economic Affairs (IEA) has advised the Bank of Ghana (BoG) to adopt a more hardline approach to inflation by, among other things, reviewing its medium-term inflation target band of 8±2 percent, which has remained static and is above the target of comparable economies.

According to the public policy think-tank, the relatively high mark within the central bank's inflation-targetting framework is indicative of the latter's seeming resolve on the subject – despite claims from the BoG that it has considered lowering its inflation target at some point.

"Regarding the inflation target, it is the case that the 8±2 percent has been in place almost forever; which, in a way, seems to suggest a lack of sufficient ambition on the Monetary Policy Committee's part to lower inflation further to levels comparable to those of Ghana's peers or trading partners," the Institute said in a statement following conclusion of the Bank MPC's 106th meeting.

In the statement, the IEA expressed satisfaction that the MPC's decision was largely in sync with its projections and recommendations prior to the meeting.

Clarification

The IEA also sought to clarify the misconception that – prior to the recent meeting – it had called for abandoning the current monetary policy framework.

It said it had called for the Bank to adopt complementary measures within its mandate, and also in conjunction with key stakeholders, particularly the fiscal authorities, due to limitations of the demand-focused strategy in taming inflation in a region where prices rise almost exclusively as a result of supply-based factors.

Additionally, transmission of the policy rate lags due to the nation's comparatively weak financial system; and as such, the benchmark rate invariably pushes lending rates artificially high – resulting in limited economic growth.

Responding to general concerns about efficacy of the monetary tool, Governor of the BoG Dr. Ernest Addision said inflation-targetting has served the country well in contributing to bringing inflation down from the high levels prior to its formal adoption in 2007.

In the 20-year period from the turn of the millennium in 2000, inflation declined from a little over 40 percent to single-digit figures by 2020 – averaging 16 percent annually.

But it is the view of the Institute that the inflation-targetting framework cannot be given sole credit for the lowered inflation since its adoption, as the economy has been generally better managed than in preceding periods – as evidenced by the improvement in all other key macroeconomic indicators.

"While the IEA recognises that inflation has been brought down progressively under inflation-targetting, it has to be noted that along with inflation almost all key macroeconomic indicators have improved during the period in question, in line with generally improved macroeconomic management of the economy," the statement read in part.

Industrialisation needed

The Institute noted that the current conversation over inflation must be looked at in the wider context of persistent macroeconomic problems of high fiscal deficits, high public debt, exchange rate instability, high rate of employment and large external imbalances, which it describes as "manifestations of a bigger problem".

"The problem is the underlying weak structure of the economy, characterised by reliance on low-value-added primary export products and high import dependency. The only way to find a durable solution to these recurrent problems is to address the economy's weak structural fundamentals," the IEA noted.

Describing industrialisation as the only permanent solution to the myriad of nagging problems, the Institute added: "This cannot, however, be achieved by relying on our narrow tax base and borrowing, but rather by leveraging our vast natural resource wealth by taking ownership of it".