The Bank of Ghana's "pro"-cedi measures: a quick analysis

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It is obvious that the measures announced yesterday by the Bank of Ghana are restrictions on foreign exchange transactions; they are, in effect, quantity (capital) controls. In any market, quantity and price are different sides of the same coin. Therefore, these quantity controls are disguised price controls intended to increase or stabilize the external price (value) of the cedi through regulatory measures instead of market-based measures.

The Bank's measures fall in two categories:

(a) measures to reduce the demand for dollars (or foreign currency): (i) ban dollarization; (ii) limit withdrawals from foreign exchange accounts, (iii) No bank shall grant a foreign currency denominated loan or foreign currency linked facility to a customer who is not a foreign exchange earner, etc etc

(b) measures to increase the supply of dollars (or foreign currency): exporters are to repatriate all their forex earnings to Ghana.

The ban on dollarization in October 2012 did not stop the depreciation of the cedi. According to the Bank's statement on Feb 5, 2012 "Bank of Ghana Notice No. BG/GOV/SEC/2012/12 dated **October 10, 2012** ... states that all transactions in the country are required to be conducted in Ghana cedis, which is the sole legal tender."

The fact that the Bank had to re-issue its warning is a clear indication that it has not been able to enforce this policy. Good luck to NOTICE NO. BG/GOV/SEC/2014/02 dated February 4, 2014. Even if the Bank can perfectly enforce this policy, it will have no effect on the value of the cedi. For the details of this argument, see my August 2012 article titled "Is banning dollarization in Ghana sound economic policy?": http://www.uoguelph.ca/~ jamegash/Dollarization.pdf

It is well-known in economics 101 that when a commodity is rationed, its price goes up. The limit on withdrawals from foreign exchange accounts is equivalent to rationing foreign exchange. If I cannot withdraw dollars from my forex account, I will use my cedis to demand dollars in the market. This will increase the value of the dollar and thus reduce the value of the cedi. The policy in a(iii) has the same effect. The policies in (a) will not reduce the demand for dollars. There is a difference between reducing the desire for a commodity and limiting the ability to acquire the commodity. The price of the commodity is what people are willing to pay (desire) at a given quantity. The policies in (a) limit the ability to acquire dollars. They do not reduce the desire for dollars (again see my article on banning dollarization at the link above).

Some have argued that in advanced countries, there are also restrictions on cash withdrawals from forex accounts. But it is important to note that these economies are cashless economies, so restrictions on cash withdrawals from forex accounts, **if they exist**, will not have the same effect as they will in an economy like Ghana where most people use cash. In fact, the BOG has not only imposed restrictions on cash withdrawals from forex accounts but also on the use of cheques: "No cheques or cheque books shall be issued on Foreign Exchange Accounts (FEA) and Foreign Currency Accounts (FCA)."

Let's consider the policy in category (b). When exporters repatriate their forex earnings to Ghana, there is an increase in the supply of dollars in Ghana. Isn't that the objective of the Bank's policy? Why is it also necessary that "upon receipt of export proceeds, the bank shall within 5 working days **convert the proceeds into Ghana cedis**."? The exporters do not want to hold their wealth in cedis. This forced conversion into cedis will reduce the return to their businesses and **reduce exports**. Not good for the Cedi. This could also lead to capital flight. You want to stabilize the cedi? But at what price/cost ...?

Things get worse. An exporters must convert his/her forex into cedis "based on the average Interbank Foreign Exchange Rate prevailing on the day of conversion with a spread **not exceeding** 200 pips." The spread is the difference between the bid and ask prices demanded by buyers and sellers respectively. A cap on the spread is, in effect, a price control measure. Are we back to the economic policies of the 1970s?

Under the Free Zone Act (1995), "There are no conditions or restrictions on repatriation of dividends or net profit; payments for foreign loan servicing; payments of fees and charges for technology transfer agreements; and remittance of proceeds from sale of any interest in a free zone investment." Our Free Zones companies are not bound by the BOG's directives.

I can see the wisdom in requiring that **some**, if not all, of export earnings should be repatriated back to Ghana. This is not unusual (e.g., see links to similar policies (current or past) in China, Nigeria, and India). What does not make sense are the additional requirements that (a) export earnings should be converted into cedis, and (b) the spread cannot exceed 200 pips. The amount to be repatriated to Ghana need not be 100%. After all, why do we allow our Free Zones companies to repatriate 100% of their dividends and net profits to foreign countries? In addition to the **numerous** tax incentives given to these companies (e.g., "100% exemption from payment of income tax on profits for 10 years and shall not exceed 8 per cent thereafter". Note that the standard corporate tax rate is 25%), do they need this perk too?

According to an article at one of the links below the "Reserve Bank of India (RBI) on 11 June 2013 raised the limit for online repatriation of export proceeds by over three-folds to 10,000 US dollars. RBI also made it mandatory to repatriate full value of exports within 12 months for units in **Special Economic Zones** (SEZs). The decision from RBI came up with the aim of arresting the rupees slide by boosting Forex inflows."

Like India, shouldn't we get more from companies in our free zones, a policy which has been in place for since 1995? How many companies are in our free zones? They are supposed to export 70% of their output? Do they?

As many have pointed out, the BOG's measures are stopgap measures. They do not address the fundamental macroeconomic and structural imbalances in the economy. That's not a job for only the BOG. The ministry of finance, Ghana Revenue Authority, all Ghanaians and the man himself, my president and your president, John Mahama must get to work. Shall we begin by cutting frivolous expenditures? Addressing members of the diplomatic Corp at Peduase Lodge, president Mahama was reported to have said that "his government "is exercising stricter financial discipline". But Mr. President, draconian economic policies and fiscal discipline are not the same things. Or do we have an independent central bank? Seriously?

Now China. The country is in an enviable position after decades of hard work. They want to reduce the flow of foreign currency into China. This is intended to slow down the appreciation of the Chinese currency and reduce excess liquidity (ah, suffer today, enjoy tomorrow). See article below.

http://www.citibank.com/ transactionservices/home/ region/asia/docs/ newadminrules_english.pdf

(CHINA): State Administration of Foreign Exchange (SAFE) has announced new administration Rules on export proceeds kept abroad for corporations registered in China (excluding those registered in China bonded areas). These new rules are to further improve the efficiency of corporate cash management on its imports/exports as well as to encourage local corporations to "go abroad".

SAFE started a trial program on October 1st, 2010 that allowed 60 exporters in four cities/provinces to keep their export proceeds abroad. This *new* regulation that became effective as of **Jan 1st 2011** is to further extend the program to all exporters nationwide.

The annual accumulated balance kept overseas for each company shall not exceed the original registered balance with SAFE.

This new practice to keep corporation's foreign currency earnings offshore has become effective sooner than previously anticipated. **It is expected to slow down current foreign currency inflows** as well as the further buildup of foreign reserves in China. With the slowdown of the two, it is expected that inflation pressures and excess market liquidity will also be reduced.

Chinese exporters get almost all their revenue in dollars and other foreign currencies (other than RMB). **In the past, they were required to bring them all back to China** and then further remit out for the import payments. With the new rule, corporations could directly use the funding kept abroad to cover the import cost.

India:
http://www.jagranjosh.com/ current-affairs/rbi-hiked-the- cap-for-online-repatriation- of-export-proceeds-1371010327- 1

Nigeria: http://www.globaltimes.cn/ business/world/2009-07/451404. html