POLICY BRIEF

MACROECONOMIC IMBALANCES AND BANK LENDING BEHAVIOUR IN GHANA

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Executive Summary

Macroeconomic imbalances as manifested through persistent inflationary pressures, exchange-rate volatility, and sustained fiscal stress, have become a defining feature of Ghana's macroeconomic environment over the past decade. While these imbalances intensified globally following the 2007–2008 financial crisis, their effects have been particularly pronounced in emerging and developing economies, where financial systems are bank-dominated and highly sensitive to macroeconomic shocks. In Ghana, the period since 2019 has been marked by severe macroeconomic disruptions that have fundamentally reshaped banking sector behavior and private-sector credit dynamics as the banking industry constitute more than 76% of the total asset base of the financial subsector with very high interconnectedness with the insurance subsector and others.

This policy brief examines the effect of macroeconomic imbalances on bank lending in Ghana, with particular emphasis on exchange-rate movements, inflation, and fiscal conditions. Bank lending behavior is analyzed through loans and advances to customers, asset quality, and banks' risk posture. Using a panel dataset covering 18 universal banks over the period 2015–2024, the study applies fixed effects and dynamic System Generalized Method of Moments (GMM) estimation techniques to account for persistence in lending behavior, endogeneity, and unobserved bank-specific heterogeneity.

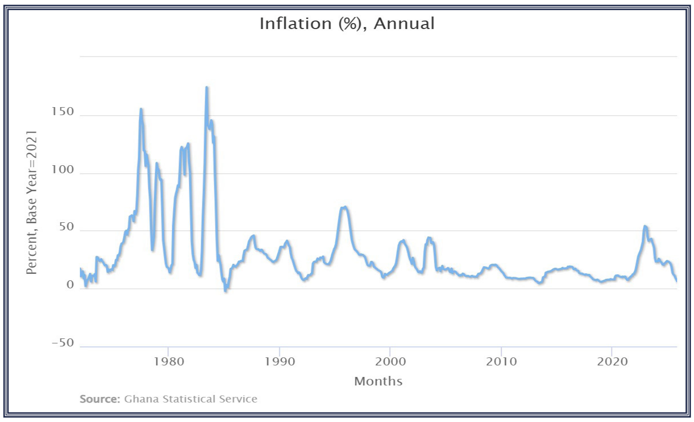
The findings show that bank lending in Ghana is highly persistent and strongly constrained by deteriorating asset quality, as reflected in elevated non-performing loans. Exchange-rate movements exert a significant influence on lending, largely through nominal and valuation effects associated with currency depreciation. Inflation and fiscal stress primarily affect lending indirectly, operating through tighter monetary conditions, higher interest rates, and heightened risk aversion. Persistent Fiscal imbalances as captured by weak primary balances and rising public debt are found to suppress bank lending by increasing macroeconomic uncertainty and reinforcing crowding-out effects.

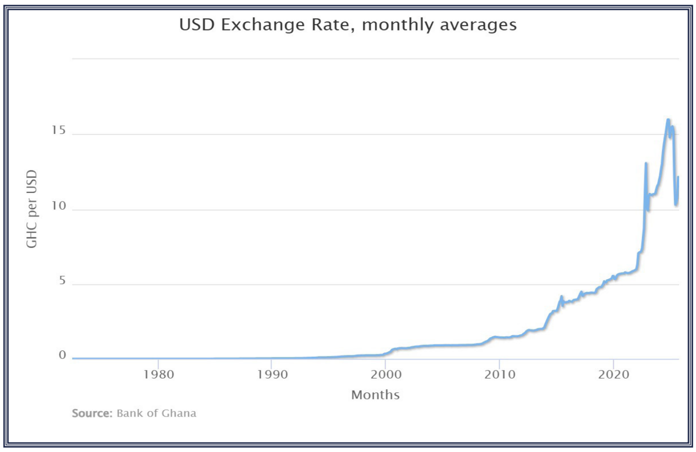
Overall, the results indicate that macroeconomic imbalances shape bank lending in Ghana more through risk management, pricing behavior, and balance-sheet adjustments than through sustained real credit expansion. The study highlights the importance of credible macroeconomic policies, fiscal discipline, and forward guidance in restoring confidence, strengthening bank risk appetite, and supporting sustainable private-sector credit growth.

1.0 Context and Importance

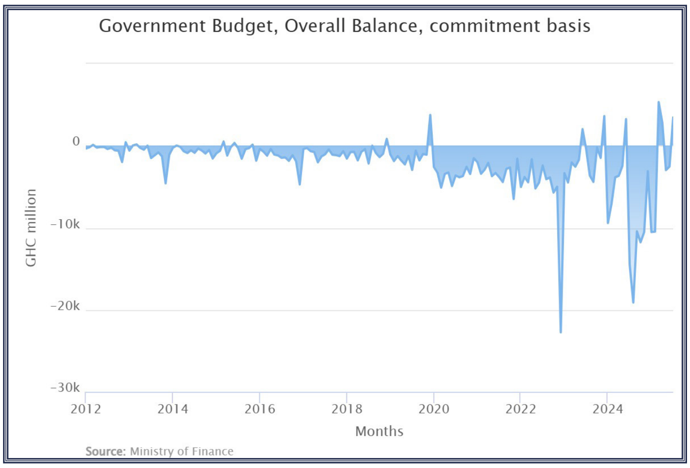
Macroeconomic imbalances have long been recognized as a major source of vulnerability for banking systems, particularly in economies where banks serve as the primary channel of financial intermediation. These imbalances disrupt the normal functioning of the economy by introducing uncertainty, weakening balance sheets, and impairing the transmission of monetary and fiscal policy. Empirical literature largely agrees that macroeconomic instability tends to reduce bank lending, although the magnitude and transmission mechanisms vary across countries depending on economic structure, institutional quality, and policy credibility.

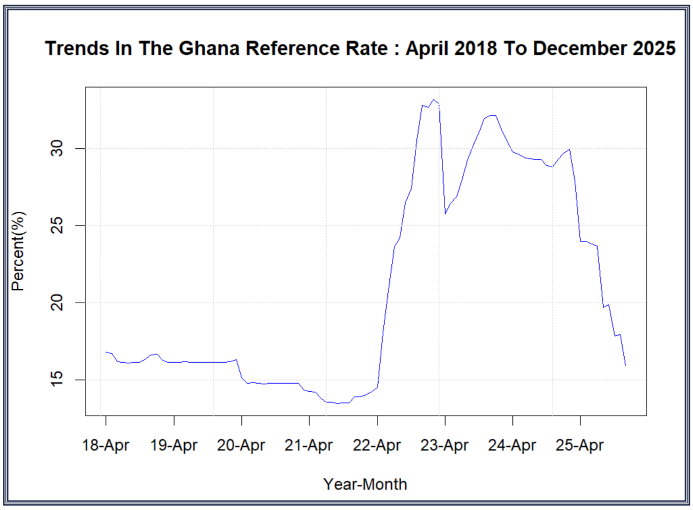
Inflation surged to a historic peak in 2022 and remained persistently above the central bank's target band through 2024. In response, monetary policy was tightened aggressively, raising funding and lending costs across the banking system. At the same time, the Ghanaian cedi experienced sharp and repeated episodes of depreciation, increasing balance-sheet risks for banks and borrowers, particularly those with foreign-currency exposure.





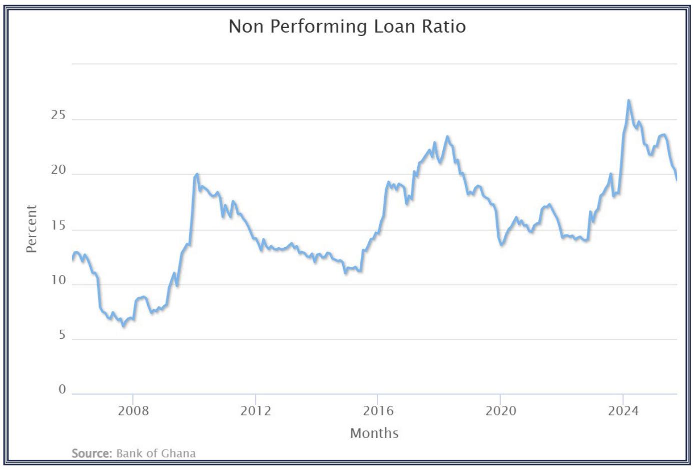
Fiscal conditions further compounded these challenges. Rising fiscal deficits, weak revenue performance, and escalating interest costs led to a rapid accumulation of public debt, culminating in debt distress and the implementation of a Domestic Debt Exchange Programme under an IMF-Extended Credit Facility (ECF) programme. While the debt restructuring was necessary to restore sustainability, it imposed significant valuation losses on banks' holdings of government securities, weakened capital buffers, and tightened liquidity conditions.

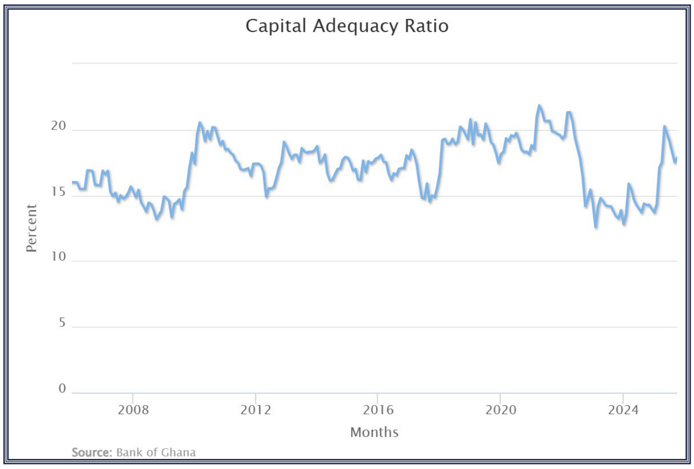




These developments are particularly important given the structure of Ghana's financial system. The banking sector accounts for more than three-quarters of total financial assets and remains the dominant source of external finance for firms, especially small and medium-sized enterprises. As such, disruptions to bank lending have direct implications for investment, employment, and economic growth.

Despite rising deposits in recent years, real private-sector credit has remained weak, raising important policy questions about the interaction between macroeconomic imbalances and bank lending behavior.





Against this backdrop, this study provides timely empirical evidence on how macroeconomic imbalances influence bank lending dynamics in Ghana, contributing to the policy debate on financial stability, credit growth, and macroeconomic management.

2.0 Methods and Empirical Approach

The study adopts a quantitative empirical methodology based on panel data analysis. The sample comprises 18 universal banks operating continuously in Ghana over the period 2015–2024, selected based on data availability and consistency. This coverage ensures broad representation of the banking system while maintaining a balance dataset.

Bank lending behavior is measured using loans and advances to customers, while asset quality and risk conditions are captured through the non-performing loans ratio and the capital adequacy ratio. Macroeconomic imbalances are proxied by movements in the exchange rate, headline inflation, the primary fiscal balance, and total public debt as a ratio of GDP. Real GDP growth is included as a control variable to capture demand-side effects.

The empirical strategy proceeds in several stages. First, descriptive statistics and correlation analysis are used to characterize the data and explore initial relationships among variables. Second, multicollinearity diagnostics are conducted using Variance Inflation Factors to ensure robustness of inference. Third, static panel models are estimated, with the Hausman specification test guiding the choice between fixed and random effects. Finally, a dynamic System GMM estimator is employed to address endogeneity, persistence in lending behavior, and unobserved bank-specific effects.

The System GMM framework is particularly appropriate in this context, as bank lending decisions are inherently dynamic and influenced by past lending outcomes, balance-sheet adjustments, and evolving macroeconomic conditions. The validity of the dynamic estimates is assessed using standard diagnostic tests, including tests for serial correlation and overidentifying restrictions.

3.0 Results and Discussion

The empirical results reveal several important patterns. First, bank lending in Ghana exhibits strong persistence, indicating that current lending decisions are heavily influenced by past lending behavior. This reflects the role of relationship banking, loan maturity structures, and gradual balance-sheet adjustment processes.

Second, asset quality emerges as a key constraint on lending. Higher non-performing loans significantly reduce banks' willingness and capacity to extend new credit, reinforcing the importance of credit risk management in periods of macroeconomic stress. Capital adequacy is also associated with more cautious lending behavior, suggesting that banks prioritize balance-sheet resilience over expansion when uncertainty is elevated.

Third, exchange-rate movements play a prominent role in shaping lending dynamics. Currency depreciation is associated with higher nominal lending, largely reflecting increased working-capital financing needs, valuation effects, and foreign-currency-linked borrowing rather than a genuine expansion in real credit. This finding highlights the distinction between nominal credit growth and real financial intermediation.

Fourth, inflation and fiscal variables exert indirect but economically meaningful effects. High inflation is associated with tighter monetary conditions and elevated lending rates, which suppress real credit demand. Fiscal stress, captured by weak primary balances and rising public debt reduces bank lending by increasing sovereign risk, reinforcing crowding-out effects, and heightening macroeconomic uncertainty.

Taken together, the results indicate that macroeconomic imbalances influence bank lending in Ghana primarily through risk, pricing, and balance-sheet channels. Nominal lending may continue to rise during periods of instability, but real credit expansion remains constrained.

4.0 Policy Implications and Recommendations

Several important policy lessons emerge from the study and warrant careful consideration.

Macroeconomic stability is a fundamental prerequisite for restoring sustainable bank lending in Ghana. Persistent inflation and exchange-rate volatility heighten uncertainty, weaken bank and borrower balance sheets, and complicate credit risk assessment. Anchoring inflation expectations through credible and consistent monetary policy remains essential, as does reducing excessive exchange-rate volatility. Clear and transparent monetary policy communication, including forward guidance, can help shape expectations, lower uncertainty, and improve banks' willingness to extend credit to the private sector.

Fiscal policy occupies a central place in the bank lending–macroeconomic nexus. Ghana's recent experience under the IMF-supported Extended Credit Facility programme highlights both the risks associated with fiscal slippages and the gains from credible adjustment. The programme has played a key role in restoring macroeconomic stability, improving policy credibility, and stabilizing financial conditions.

However, the period approaching programme exit is particularly delicate. Prudent fiscal management must remain a priority to ensure that the economy does not relapse into large deficits, unsustainable debt accumulation, and renewed pressures on the banking system. Sustaining the gains achieved under the IMF programme will require firm commitment to expenditure discipline, strengthened domestic revenue mobilization, and adherence to clearly articulated fiscal consolidation paths.

Strengthening bank balance sheets is also critical for improving lending capacity. Elevated non-performing loans continue to constrain credit supply by increasing provisioning needs and reinforcing risk aversion. Addressing legacy asset quality challenges, enhancing credit underwriting standards, and strengthening recovery and resolution frameworks will support healthier bank balance sheets and improve lending resilience over the cycle. At the same time, sound capital planning under stress conditions can help banks absorb shocks without excessively curtailing credit.

Policy coordination further enhances these efforts.
Effective alignment between monetary, fiscal, and financial sector policies reduces uncertainty and improves the overall effectiveness of macroeconomic adjustment. When policy actions are coherent, predictable, and mutually reinforcing, banks are better positioned to support private-sector investment, economic diversification, and long-term growth, rather than adopting overly defensive balance-sheet strategies.

5.0 Conclusion

This policy brief provides empirical evidence that macroeconomic imbalances have played a central role in shaping bank lending dynamics in Ghana over the past decade. Inflation, exchange-rate volatility, and fiscal stress interact with bank balance sheets and risk behavior to constrain real credit expansion, even when nominal lending appears to grow.

The findings underscore that restoring sustainable bank lending requires more than liquidity or capital alone. It requires credible, predictable, and coordinated macroeconomic policies that reduce uncertainty, strengthen confidence, and allow banks to support private-sector investment and long-term economic growth.

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