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In partnership with The MasterCard Foundation

Impact of Ghana's economic slowdown on Habitat's Building Assets, Unlocking Access project

When Habitat for Humanity launched the Building Assets, Unlocking Access project in 2012, Ghana was at the top of the list of countries that appeared poised to adopt such a program based on selection criteria including:

- A growing and relatively stable economy, and a political climate that favors investment.
- Increasing regulation in the microfinance sector that hints of future consolidation among institutions.
- High demand for housing microfinance, given that up to 90 percent of the housing stock is self-built.
- Positive preliminary conversation between Habitat for Humanity International and two major microfinance institutions.

When the project started in 2012, it had to rely on data from late 2011 or early 2012, when Ghana's economy was still booming. In fact, the economy had already started to collapse, but that would not be evident for several months after the project began. This period of economic slowdown was accompanied by an alarming rise in interest rates. The Bank of Ghana's benchmark lending rate doubled between 2011 and 2015, rising from 12.25 to 25 percent. The timing could not have been worse.

With support from Habitat's Center for Innovation in Shelter and Finance, two financial institutions (one bank and one savings and loan company) worked throughout 2013 to develop a housing microfinance product. However, when the products were ready to be launched in 2014, the borrowing rate for microfinance institutions had risen to 38 percent, and the deteriorating economic environment in Ghana had dramatically raised the risk premium of launching a new product. The financial institutions were unable to shift increasingly costly capital to the new product. They needed access to longer-term capital with stable pricing, but capital access was not a feature of the project. With no clear sense of when the product would be launched, the project was closed in Ghana. Although several factors contributed to this reversal (which are documented in the project's midterm evaluation), the most obvious is the economy.

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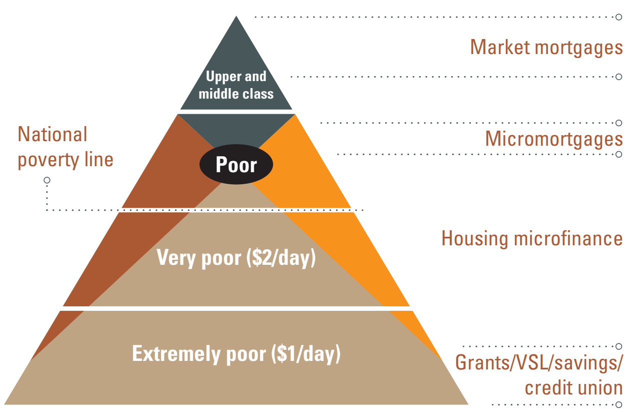
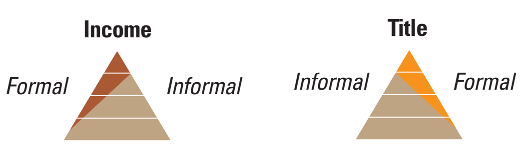
Background

- In 2012, Ghana was coming to the end of a period of rapid economic growth built largely on new oil wells that had come into production in 2010. Pre-election largesse drove up fiscal spending in advance of the 2012 voting, deepening a deficit that had appeared to be improving. At the same time, falling commodity prices were taming the unprecedented growth rates of 2010-11. Against the backdrop of a currency whose value was falling precipitously, rising fiscal and current account deficits drove a period of economic decline that bordered on a crisis by the end of 2014.

- Meanwhile, microfinance institutions in Ghana were improving financial inclusion by diversifying their product offerings. Insurance and a variety of consumer loans were the first products that microfinance institutions added, but housing was a recognized need. In 2013, Habitat for Humanity and The MasterCard Foundation teamed up to help microfinance institutions develop new housing loans. Based on the sound economy and vibrant microfinance sector, Ghana was an obvious choice to begin the project.



Sample developing economy country profile



Housing microfinance loans allow families to build the value of their main asset: their home.

Building Assets, Unlocking Access is a project that helps African banks and other financial service providers build their capability to offer housing microfinance products. Ghana was selected for the project in 2013, but the project closed there in 2014.

Ghana's economy was the fastest-growing in the world in 2011, but by 2014 it had deteriorated and needed a bailout from the International Monetary Fund.

Note that the rust-shaded area of the pyramid represents the population with documentable income, and the gold-shaded area represents the population with formal title to their property.

Highlights

2012 – Ghana is positioned for growth and diversification of products.

2013-14 – **The squeeze:** High inflation and devaluation lead to reduced liquidity for microfinance institutions because of:

- An appreciating dollar and falling commodity prices.
- Fitch's downgrading of Ghana's rating to B- with a stable outlook and a fiscal deficit in October 2013.
- The requested IMF bailout in August 2014.

2015 – Mixed developments:

- Ghana reaches an IMF deal for $1 billion.
- Ghana's currency, the cedi, hits its all-time low in June.
- Donors resume budget support in July.
- Fitch downgrades Ghana to B- in October.
- General election set for 2016.

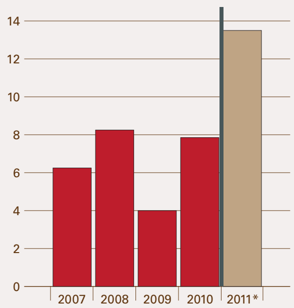
In this environment, microfinance institutions can launch a new product only if long-term, low-cost funds are made available.

Lessons

- Projects that rely on injections of capital from financial institutions are at risk from changes in the economy.
- Establishing a contingency to pause a project may help protect the anticipated social benefits and should be explored.

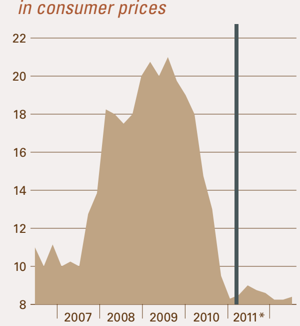
Ghana's economy 2007-11

GDP GROWTH
Annual percentage change

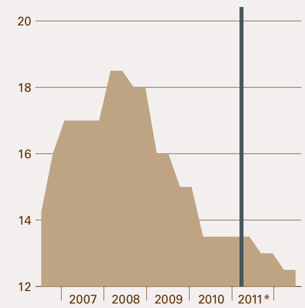


BUDGET DEFICIT
As percentage of GDP

INFLATION
Annual percentage change in consumer prices



BANK OF GHANA INTEREST RATE
Percent



Oil production begins

Sources: IMF; Thomson Reuters Datastream

** Forecast*

> *"Ghana is the fastest growing economy in the world this year, expanding at a forecast 13.6 percent."*

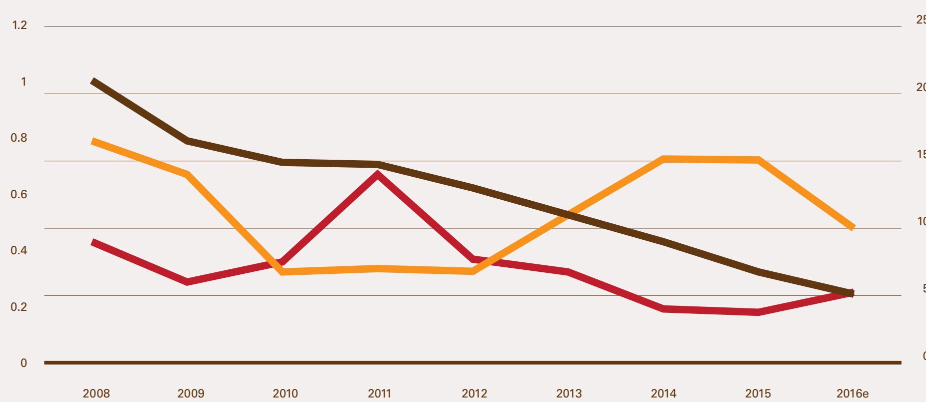
Strong gross domestic product growth, reduced budget deficits and a taming of inflation resulted in Ghana's becoming symbolic of a new African economic confidence. Newspaper headlines at the time heralded this new reality.

Unfortunately, Ghana could not sustain these gains. Spending soared before the 2012 elections at a time when commodity prices were falling; Ghana's newfound oil was worth less every year. Current account deficits and high inflation pushed its currency, the cedi, to new lows and interest rates to new heights. By 2015, the headlines had changed:

> *"Ghana remains well short of solidifying the foundations of macroeconomic fundamentals necessary for sustained growth and prosperity."* - Index of Economic Freedom

Ghana's economic slowdown

As Ghana's economic woes forced interest rates ever higher, microfinance institutions scaled back expansion, new products and inclusion. The housing microfinance product stalled, and the project closed.



GDP, percentage change *Inflation, percentage change* *Cedi vs. U.S. dollar*

Learning from the Ghana experience

The Building Assets, Unlocking Access project in Ghana began with a promising financial environment, commitments from two financial institutions to develop housing microfinance products, potential longer-term funding from MicroBuild (a wholesale lender dedicated to housing microfinance), and a team ready to support the project implementation. Even under optimal conditions, launching a new product is risky. But a deteriorating economy and the dramatically rising cost of capital (including MicroBuild, which lends in hard currency), resulted in an environment where launching a new product with funds borrowed at high interest rates was even riskier. Ultimately, the risk was greater than the financial institutions could comfortably bear. Could the project have been protected from the collapse of the cedi, spiraling budget deficits and falling commodity prices that created an inflationary environment and soaring interest rates? No, but perhaps that is the wrong question.

Every economy is at the mercy of the business cycle and periods of rapid growth and decline. But in almost all cases, the pendulum eventually swings the other way. How should development programs working with the private sector deal with these cycles? While Ghana continues to face a difficult macroeconomic environment, it is still growing at rates that would be very welcome by most industrial economies – around 4 percent last year. The IMF bailout will help reduce the budget deficit and should lead to increased investment in infrastructure, boosting the economy. Though commodity prices have remained stubbornly low, they will have to rebound at some point. Restoring value to the cedi and bringing interest rates down could take longer, but the crisis will eventually come to an end. When it does, there will be a new outlook for the government of Ghana, its creditors and the banking system. It could also have been good news for the Building Assets Unlocking Access project in Ghana, had the project not closed early in 2015. This is especially true since economic uncertainty, inflation and large balance sheet write-offs in the wake of the economic downturn are all likely to push banks to focus more on short-term financing, such as products for incremental housing, rather than on long-term products such as mortgages. However, without locally denominated funds and continued technical assistance to launch the housing microfinance products developed through the Building Assets, Unlocking Access project, they will likely be mothballed.

The imperatives of a funded project created a no-win situation in light of Ghana's new economic reality. The project's staff, driven by deliverables and deadlines, believed the financial institutions should launch the product, high interest rates notwithstanding. The financial institutions believed they were being asked to compromise their business priorities at a difficult time. Is this the inevitable outcome of a project with milestones and deadlines when faced with a shift in the external environment? Or would it be possible to pause the project until economic conditions are more favorable to the development of housing microfinance?

Projects that rely on injections of capital from financial institutions are inherently at risk from changes in the economy, particularly rate changes, which can jeopardize anticipated social gains. Establishing a contingency to pause a project and wait out the business cycle, or establishing a contingent facility to reduce risk to the financial institution if the economic environment deteriorates, may help protect the anticipated social benefits and should be explored.

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