'Dutch Disease' Imminent - As Ghana Enters Oil Economy

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The Centre for Policy Analysis (CEPA) has warned of dire economic consequences if the Ghana Cedi is pegged at equal value to the major international currencies.

Executive Director of the Policy think tank, , expressed the fear that the country risk suffering from the 'Dutch Disease', a variant of the resource curse, if the county's currency, the Ghana Cedi was equated to the dollar, Euro and Pound sterling.

Dr Abbey's warning comes at a time the cedi is inching up against the major international currencies which some analysts have hailed as neccessary for the much needed turn-around the country so badly needs.

But at the launch of its recent publication in Accra, Dr Abbey said the desire of policy makers to peg the exchange of the Ghana Cedis in parity to the US dollar would be the beginning of the Dutch Disease.

According to the CEPA boss, there are already signs of the cedi appreciating against key currencies in the first quarter of the year, which is expected to continue for the rest of the year.

"This steady and creeping appreciation of the cedi comes with associated risks of choking off the growth and employment potentials of non-oil sectors, in particular, agriculture and manufacturing"' he said.

"As Ghana enters the oil era, an exchange rate effect symptomatic of the Dutch Disease is expected", the CEPA boss added.

The publication which was titled 'The year 2010, From a Cocoa Economy to an Oil Economy', details how the various sectors of the economy will fare when the oil begins to flow later this year.

The Dutch disease is so named because of the destructive effect on growth and employment potential in the non oils sectors of the Dutch economy at the discovery of substantial gas reserves in the 1960s.

It is a form of a resource curse, which originated from the nominal and appreciation of the exchange rate that resulted from the large inflows of foreign exchange earnings from the Dutch export of gas.

Over the years, successive governments have campaigned for the increased base of the

country's non-traditional exports in order to maximize the foreign exchange earnings of the country to shore up the country's currency.
This year the first of Ghana's 3.2 billion barrels will begin to flow from its waters and it is expected that the expected inflows will fill the foreign exchange gap that the country requires so badly.

Dr Abbey contends that the effective management of the exchange rate would be critical if oil is to enhance the country's growth prospects and to avoid the ills of the Dutch Disease.

"The lessons from the experiences of other African oil producers, in which windfalls in foreign exchange earnings have had a number of negative economic repercussions, need to be fully learnt," Dr Abbey added.

The exchange rate effect, together with the yield on Ghana's Eurobond source of information on the country risk premium on Ghana and the rate of inflation would be key considerations in the deliberations of the Monetary Policy Committee (MPC) of the Bank of Ghana (BOG) for the determination of both the real and nominal policy rate (prime rate).

He said developments on the foreign exchange market front were the exact opposite of what was currently going on in China.

According to him, while the Chinese appeared willing to sacrifice a measure of current well-being in exchange for jobs, Ghana, a much poorer country, appeared bent on choosing a preference for current well-being even at the expense of having less jobs.

Chinese policymakers do not use the yuan as a tool for managing inflation, "they use it instead as tools to maximise export and employment, a tool they appear not yet ready to give up," Dr Abbey said.

China is seen to have kept the value of its currency artificially cheap, thus implicitly subsidising its exports while taxing its imports.

This means that the appreciation of the exchange rate means loss of price competitiveness of domestic products on the international market.

Comparatively, made-in-Ghana exports would be over-priced in foreign markets when the Ghana Cedi is at par with major trading partners' currency.

This would mean a squeeze on profits initially, then a loss of market share and finally to cutbacks in domestic production and job losses.

On the import side, goods coming into Ghana will become increasingly cheaper than their substitutes made in Ghana. Again initially this will place a squeeze on profits of domestic producers engaged in activities that compete with commercial importing.

If this is not quickly rectified it will ultimately lead to the collapse of such domestic productive activities with consequent job losses.