Author: Freedom Giant Selorm Omega
Date: 7th July, 2025

THE ECONOMICS OF CURRENCY FLUCTUATION

1.0 Background

In an open economic system, currency fluctuation denotes the variation in the relative value of one currency against another, a phenomenon fundamentally propelled by the forces of supply and demand within the foreign exchange market. The prevailing strength or weakness of a nation's foundational economy typically serves as the primary determinant of its currency's exchange rate. Consequently, these dynamic movements exert considerable influence across a spectrum of macroeconomic variables, including trade competitiveness, inflation, investment patterns, external financial relations, commercial activity, economic growth trajectories, capital flows, the burden of debt servicing, prevailing interest rates, and overarching macroeconomic stability. Thus, for both advanced and developing economies, a comprehensive grasp of the underlying economics of exchange rate volatility is an indispensable prerequisite for the formulation of robust monetary, fiscal, and trade policies.

2.0 Exchange Regimes and Currency Fluctuation

2.1 Currencies

The currency used by various countries differs across the world. As some countries ascribe to a common currency of their bloc (Eg, European Union and CFA Zone countries in West Africa), the majority of countries use differentiated currencies (Eg, Pounds, Ghana Cedis, Yen, Rand, etc.). Despite these differences and their related impact on trading, the world has standardised currencies for global transactions (Use of dollar). This standardisation occurred against the backdrop of the failure of the gold standard, due to protectionism, currency devaluation, and mass unemployment and economic depression in the 1990s. These currencies appreciate or depreciate relative to the dollar (Standard currency) depending on the strength of the host country's currency.

Table 1: Currencies and Currency Fluctuation

Country	Continent	Currency	Average Value (per USD)	Currency Fluctuation
USA	North America	US Dollar (USD)	Base Currency	Relatively stable
Ghana	Africa	Ghana Cedis (GHC)	1 USD≈ 12.5 GHS	High volatility; sharp depreciation in 2022, partial recovery in 2025
Nigeria	Africa	Naira (NGN)	1 USD≈ 1500 Naira	Very high; frequent depreciation and dual rates until 2023
South Africa	Africa	Rand (ZAR)	1 USD ≈ 18.5 ZAR	Moderate; influenced by global commodity prices and politics
UK	Europe	British Pound (GBP)	1 USD ≈ 0.78 GBP	Moderate; impacted by Brexit and, inflation

Eurozone	Europe	Euro (EUR)	1 USD ≈ 0.93 EUR	Moderate; stable within EU
Japan	Asia	Japanese Yen (JPY)	1 USD ≈ 155 JPY	Moderate–high; sensitive to interest rate changes
India	Asia	Indian Rupee (INR)	1 USD ≈ 83 INR	Moderate; depreciating trend
China	Asia	Chinese Yuan (CNY)	1 USD ≈ 7.25 CNY	Low–moderate; tightly regulated
Brazil	South America	Brazilian Real (BRL)	1 USD ≈ 5.3 BRL	Moderate; driven by political and commodity cycles

NB: Average value expected by the close of 2025 according to World Bank and IMF projections

Currency Fluctuation considers the last 3–5 years' performance, including events like inflation, devaluations, and monetary reforms.

Source: World Bank (2025) & IMF (2023)

2.2 Types of Exchange Regimes

Various countries adopt various exchange regimes to suit their economic needs. These economic needs include: economic structure, macroeconomic goals, institutional capacity, and exposure to external shocks. Large and more diversified countries (UK, Europe, Japan and USA) are most likely to use the free float regime, which allows for the interaction of the forces of demand and supply. For commodity-dependent economies like Ghana, the managed float is used, where the exchange rate is mostly determined by market forces, but the central bank intervenes occasionally to stabilise the currency or achieve economic goals. While small open economies, countries with a history of high inflation and policy credibility needed (Eg, Ecuador, El Salvador, Hong Kong, Estonia, Zimbabwe) adopt the peg (fixed or crawling peg), dollarisation or currency board. Despite these, some countries prefer the use of a mixture of regimes for financial openness.

Table 2: Types of Exchange Regimes

Regime	Flexibility	Control	Example
Fixed (Pegged)	Low	High	CFA Zone countries in West Africa, Saudi Araba
Floating (Free)	High	Low	USA, Euro zone countries, Japan
Managed Float	Medium	Moderate	Ghana, India, South Africa
Crawling Peg	Medium	Moderate–High	China (historically)
Currency Board	Very Low	Very High (Rigid)	Hong Kong
Dollarization	None	None (fully external)	El Salvador, Zimbabwe
Dual Exchange Rate	Artificial	High (manipulated)	Venezuela

Source: World Bank (2024)

3.0 Ghana's Case

3.1 History of Currency Fluctuations in Ghana

During the post-independence era (1957-1967), Ghana used the Ghanaian pound, which was the equivalent of the British pound sterling. The economy was relatively stable and characterized by a strong export sector and foreign reserves. By 1965, Ghana transitioned to the use of the cedis. Between 1965-1983 (First Cedi era), the country adopted the fixed peg regime as a result of the

1967 coup. The coup led to the devaluation of the cedi by 30%. Other factors that led to the devaluation were the decline of cocoa prices, fiscal mismanagement, rising inflation and massive parallel market activities. The third era (1983-2006), Economic Recovery Programme (ERP) saw Ghana move to the use of the floating exchange regime. This was a result of the adoption of the Structural Adjustment Programme (SAP) with IMF support in 1983. The programme led to the regular devaluations and liberalisation of the forex market. Despite the programme, inflation exceeded 40% and massive depreciation occurred, reflecting structural weaknesses within the system and high debt levels. In 2007, the second cedis era started. The era saw the redenomination of the cedis to simplify transactions and restore confidence in the Ghana cedis. Post-redenomination depreciation era (2008-2014) saw the cedi initially stable but started depreciating after 2012. This was caused by a high fiscal deficit, current account imbalance, rising public debt, and import dependence. Again, the IMF bailout era I (2015-2019) saw Ghana enter an IMF extended credit facility aimed at fiscal consolidation and inflation targeting. Despite the reforms, the cedi faced speculative attacks, weak reserves and rising Eurobond dependence. Furthermore, 2020-2022 was considered the COVID-19 and debt crisis. The period was characterised by COVID-19 fiscal pressure, high external debt, investor exit from bonds, delay in IMF support and credit downgrades. The current period IMF bailout II (2023-2025) is characterised by debt restructuring, inflation control measures and fiscal tightening, with the managed float exchange rate regime being used.

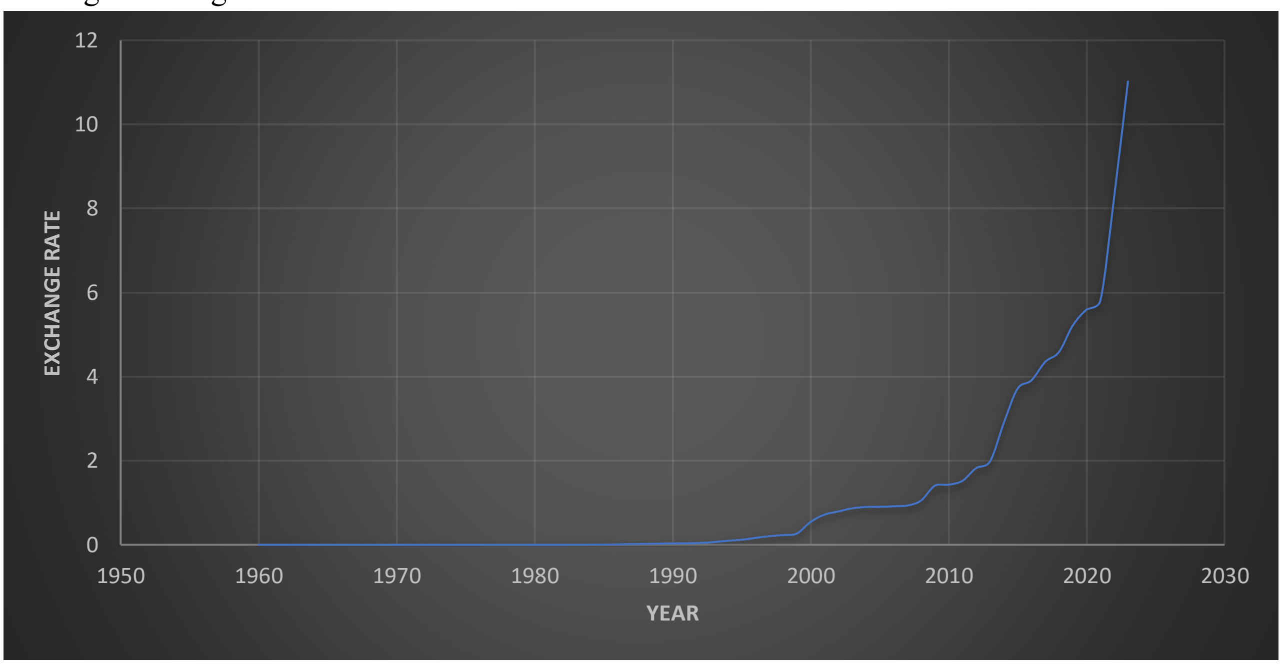


Figure 1: Currency Fluctuations in Ghana (1960-2024)
Source: World Bank (2025)

3.2 Currency Fluctuations Impact on the Ghanaian Economy

3.2.1 Exchange Rate and Inflation Rate

The Exchange Rate and Inflation Rate (2007–2025) graph provides compelling empirical evidence of the intertwined and often challenging dynamics of currency fluctuations and inflation in Ghana. The consistent long-term depreciation of the Cedi, punctuated by periods of sharp decline, has frequently coincided with significant inflationary pressures, particularly evident in the 2019-2022 period. This strong relationship indicates the critical importance of effective macroeconomic management, including prudent fiscal policies, robust monetary policy frameworks, and structural reforms aimed at diversifying the economy and enhancing its resilience to both domestic and external shocks. Addressing these fundamental issues is paramount for achieving sustained currency stability, controlling inflation, and ultimately fostering inclusive economic growth and improved living standards for all Ghanaians.

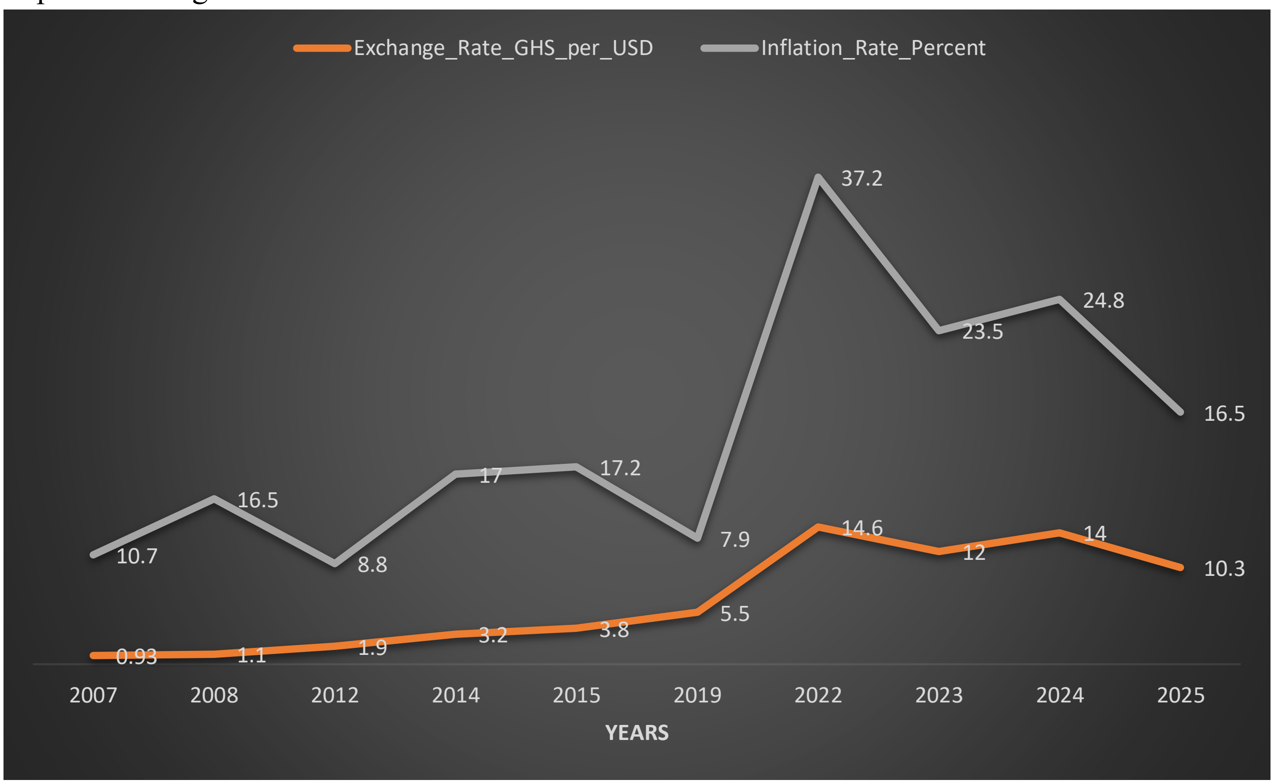


Figure 2: Ghana's Exchange Rate and Inflation rate Relationship (2007-2025)
Source: IMF Inflation Outlook reports (2007–2025)

3.2.2 Exchange Rate and GDP Growth

A rising debt-to-GDP ratio fundamentally signals diminished long-term fiscal sustainability, indicating potential governmental challenges in meeting debt obligations. Elevated public debt often leads to increased borrowing costs, as investors demand higher premia to compensate for heightened default risk. Furthermore, a substantial debt burden curtails fiscal space, limiting public investment in critical sectors such as infrastructure, education, and healthcare. This precarious fiscal position intensifies during economic downturns, where slower growth impedes debt servicing and amplifies vulnerability to external shocks.

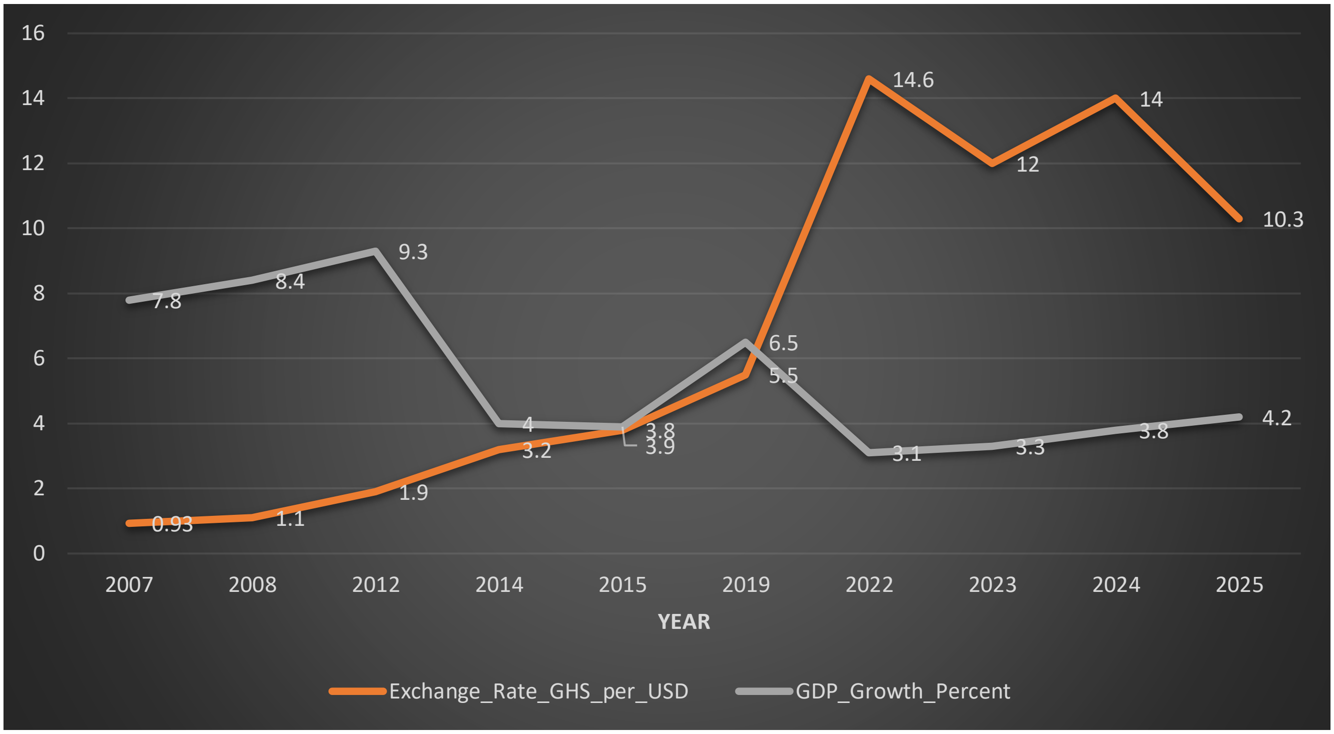
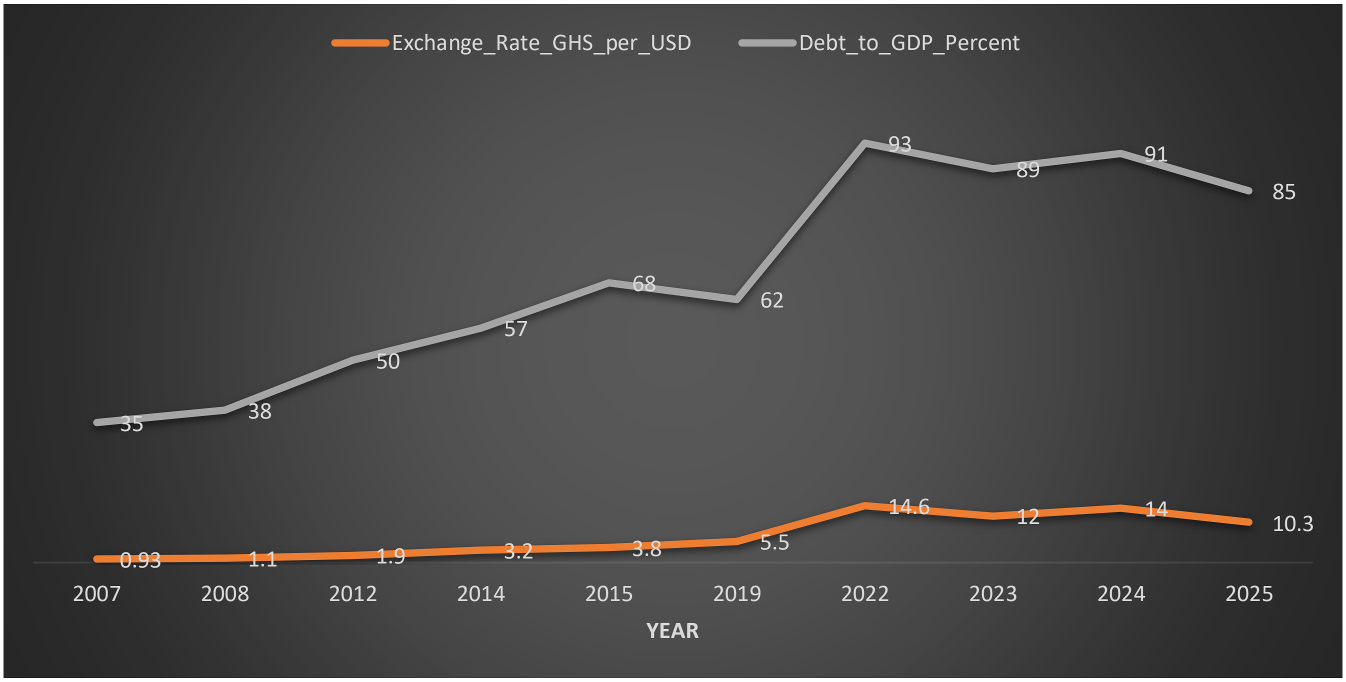


Figure 3: Ghana's Exchange Rate and GDP Growth rate Relationship (2007-2025)
Source: IMF Inflation Outlook reports (2007–2025)

A salient trend in Ghana's recent economic history is the inverse correlation between sharp Cedi depreciation and Gross Domestic Product (GDP) growth. For instance, the rapid Cedi weakening between 2019 and 2022 coincided with a marked economic deceleration, suggesting that pronounced currency depreciation can severely impede economic activity through increased import costs for firms, reduced investor confidence, and elevated debt servicing expenditures. Conversely, the 2007–2012 period exhibited a divergence, with robust GDP growth occurring concurrently with gradual Cedi depreciation. This implies that mitigating factors, such as commodity price booms and robust sectoral expansion, may have attenuated the adverse effects of currency depreciation during that phase. These contrasting patterns indicates the inherent complexity of macroeconomic management and the pivotal role of sound fiscal and monetary policy. Sustaining economic growth amidst accumulating debt and exchange rate pressures necessitates prudent debt management and concerted efforts to maintain currency stability.

3.3.3 Exchange Rate and Debt to GDP

Ghana's external debt, predominantly denominated in U.S. dollars, becomes increasingly burdensome to service as the Cedi depreciates, thereby imposing significant strain on government finances. This persistent depreciation not only inflates the local currency value of foreign debt but also erodes investor confidence, potentially precipitating capital flight and exerting further downward pressure on the exchange rate. While a weaker Cedi might theoretically enhance export competitiveness and boost foreign exchange earnings, it simultaneously escalates import costs, contributing to higher inflation, a particularly challenging issue for Ghana's import-dependent economy.



Source: IMF Inflation Outlook reports (2007–2025)

This dynamic was markedly evident between 2019 and 2022, when steep currency depreciation coincided with a substantial surge in the debt-to-GDP ratio, indicating that exchange rate depreciation was a key determinant of Ghana's deteriorating debt metrics during that period5. Furthermore, high and volatile GDP growth rates introduce economic uncertainty, complicating business planning and investment6. These fluctuations frequently stem from external shocks, such as shifts in commodity prices (e.g., oil and cocoa), global economic conditions, and investor sentiment, and can also reflect the efficacy of governmental policies aimed at fostering stable economic growth7. Stabilizing the Cedi is essential for mitigating debt-related risks, while simultaneously reducing the debt-to-GDP ratio can bolster investor confidence and contribute to exchange rate stability.

4.0 Conclusion and Recommendations

Ghana's macroeconomic trajectory since independence, particularly from 2007 to 2025, consistently demonstrates a complex and persistent interplay among currency fluctuations, inflation, economic growth, and public debt. The Ghanaian Cedi has experienced sustained long-term depreciation, with notable sharp declines, especially between 2019 and 2022, serving as a significant catalyst for macroeconomic instability. Empirical evidence robustly confirms that Cedi depreciation directly and substantially fuels inflation, primarily through elevated import costs within Ghana's import-dependent economy, as vividly illustrated by the severe inflationary spike coinciding with rapid currency weakening during 2019-2022. Moreover, the analysis frequently reveals an inverse relationship between Cedi depreciation and GDP growth, where sharp currency declines often correlate with significant economic slowdowns, attributable to rising business import costs, eroded investor confidence, and increased debt servicing burdens. Based on the empirical findings and observed macroeconomic relationships, the following recommendations are proposed;

1. Strengthening fiscal discipline and debt management is crucial. The government should reduce fiscal deficits through consistent and credible fiscal consolidation efforts, which include rationalizing public expenditures and enhancing domestic revenue mobilization.
2. The effectiveness of monetary policy should be enhanced. The Bank of Ghana must continue to focus on price stability as its primary mandate.
3. Promoting economic diversification and value addition is essential to reduce Ghana's vulnerability to global commodity price fluctuations.
4. Improvements in Ghana's structural and institutional frameworks are necessary to support private sector growth and economic transformation. Reforms aimed at enhancing the ease of doing business are needed to attract stable foreign direct investment (FDI) and stimulate domestic enterprise development.
5. Ghana should continue to engage constructively with international financial institutions such as the International Monetary Fund (IMF) and the World Bank, as well as with other development partners.