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ABBREVIATIONS

ACH	**Automated Clearing House**
AfDB	**African Development Bank**
ADV	**Advances**
AFF	**Agricultural Finance Facility**
AFI	**Alliance for Financial Inclusion**
AFREXIMBANK	**African Export and Import Bank**
AFRITAC	**Africa Technical Assistance**
AML	**Anti-Money Laundry**
APS	**Annual Provider Survey**
ATM	**Automated Teller Machines**
BN	**Billion**
BOP	**Balance of Payments**
BSD	**Banking Supervision Department**
CAR	**Capital Adequacy Ratio**
CBs	**Community Banks**
CBN	**Central Bank Nigeria**
CDD	**Customer Due Diligence**
CET	**Common External Tariff**
CFT	**Combating the Financing of Terrorism**
COMFI	**Credit Only Microfinance Institutions**
COVID 19	**Corona Virus Disease**
CPS	**Consumer Protection Section**
CRB	**Credit Reference Bureau**
CRR	**Cash Required Reserves**
DB	**Defined Benefit**
DLT	**Distributed Ledger Technology**
DSTI	**Directorate of Science, Technology and Innovation**
DTMFI	**Deposit Taking Microfinance Institutions**
EA	**Euro Area**
ECB	**European Community Bank**
ECOWAS	**Economic Community of West African States**
EFT	**Electronic Funds Transfer**
EMDES	**Emerging Market Developing Economies**
ETLS	**ECOWAS Trade Liberalization Scheme**
EU	**European Union**
EURO	**European Currency**
EVD	**Ebola Virus Disease**
FATF	**Financial Action Task Force**
FIU	**Financial Intelligence Unit**
FMD	**Financial Markets Department**

FSA	**Financial Services Association**
FSAP	**Financial Sector Assessment Program**
FSD	**Financial Stability Department**
FSDP	**Financial Sector Development Plan**
FSI	**Financial Soundness Indicators**
FSR	**Financial Stability Report**
FSSR	**Financial Sector Stability Review**
FX	**Foreign Exchange**
G2P	**Government-to-People**
GDP,	**Gross Domestic Product**
GFSR	**Global Financial Stability Report**
GIS	**Geographic Information System**
GSE	**Ghana Stock Exchange**
HHI	**Herfindahl-Hirschman Index**
HIPC	**Highly Indebted Poor Countries**
IADI	**International Association of Deposit Insurers**
IDA	**International Development Association**
IFC	**International Finance Corporation**
IFRIC	**International Financial Reporting Interpretation Committee**
IFRS	**International Financial Reporting Standards**
IMF,	**International Monetary Fund**
KPIs	**Key Performance Indicators**
KYC	**Know Your Customer**
LCR	**Liquidity Coverage Ratio**
LE	**Leones**
LIC	**Low-income countries**
LHS	**Left Hand Side**
LLP	**Loan Loss Provision**
LMAP	**Liquidity Matching Assets Profile**
LOD	**Law Officers Department**
LTAP	**long term asset profile**
LTD	**Loan To Deposit**
MDA	**Ministries Departments and Agencies**
MFIs	**Micro-Finance Institutions**
MIX	**Microfinance Information Exchange**
MMP	**Mobile Money Providers**
MPR	**Monetary Policy Rate**
MSME	**Micro, Small, and Medium Enterprises**
MTI	**Ministry of Trade and Industry**
NAC	**National Approval Committee**

NASSIT	**National Social Security Insurance Trust**
NATCOM	**National Telecommunications**
NCCUA	**National Cooperative Credit Union Association**
NCRA	**National Civil Registration Authority**
NDA	**Net Domestic Assets**
NDIP	**National Digital Identity Platform**
NFA	**Net Foreign Assets**
NFLE	**National Financial Literacy Framework**
NFLF	**National Strategy for Financial Inclusion**
NGO	**Non-Governmental Organization**
NPLs	**Non-Performing Loans**
NSE	**New York Stock Exchange**
NSFI	**National Strategy for Financial Inclusion**
OFISD	**Other Financial Institutions Supervision Department**
OSS	**Operational Self Sufficiency**
P2G	**Person to Government**
P2P	**People to People**
PAPSP	**Pan African Payments And Settlement Platform**
POS	**Point of Sales**
PPG	**Public and Public Guaranteed**
Proj aes	**Projection of Advanced Economies**
Proj EA	**Projection of European Area**
Proj EMDES	**Projection of Emerging Market and Developing Economies**
Proj W	**Projection of the World**
Q4	**Quarter four**
QAERP	**Quick Action Economic Recovery Programme**
RHS	**Right Hand Side**
RM	**Reserve Money**
ROA	**Return on Assets**
ROE	**Return on Equity**
RTGS,	**Real Time Gross Settlement**
RWA	**Risk Weighted Assets**
SAR	**Special Administrative Region**
SDF	**Standing Deposit Facility**
SDR	**Special Drawing Rights**
SIC	**Standard Interpretation Committee**
SLDPS	**Sierra Leone Deposit Protection Scheme**
SLF	**Standing Lending Facility**
SLIACO	**Sierra Leone Insurance Association of Compliance Officers**
SLICOM	**Sierra Leone Insurance Commission**

SSA	**Sub-Saharan Africa**
TA	**Technical Assistance**
TRN	**Trillion**
TSA	**Treasury Single Account**
TSX	**Toronto Stock Exchange**
UK	**United Kingdom**
UNCDF	**United Nations Capital Development Fund**
USA	**United States of America**
USD	**United States Dollar**
WAMI	**West Africa Monetary Institute**
WAIFEM	**West African Institute For Financial and Economic Management**
WAMZ	**West African Monetary Zone**
WEO	**World Economic Outlook**
WEBGIS	**Web Geographic Information Systems Resource**

GOVERNOR'S FOREWORD

The Bank of Sierra Leone (BSL) is pleased to present the fourth edition of the Financial Stability Report to the public. The Report highlights and discusses financial stability issues domestically as well as global developments that impact on the stability of Sierra Leone financial system. The BSL financial stability mandate is encapsulated in the Bank of Sierra Leone Act, 2019. A stable and sound financial system is essential for sustainable economic development and improved social welfare. Furthermore, the financial system is the vehicle through which most transactions are conducted in the real economy of Sierra Leone.

In spite of the challenges posed by the ongoing COVID-19 pandemic, the financial system in Sierra Leone still remains resilient to both domestic and external shocks. The sector recorded a relatively robust performance in 2020, although the COVID-19 pandemic is continuing. Banks were proactive to put in place business continuity measures to stem infection in their premises whilst facilitating the smooth flow of banking business. Consequently, the total assets of the financial system increased by 30.0 percent in 2020 representing 42.14 percent of Gross Domestic Product (GDP). It is important to note that most of the growth in banking sector total assets reflected lending to government (i.e. buying 1 year T-bills). This was necessary in the short run to help finance widening government deficit to deal with COVID-19 shock – but over medium term need to reduce this banking sector concentration risk and significantly increase private sector credit to support higher and more inclusive growth. Domestic deposits continue to grow and remain the main source of banks' funding, which reduces the banking sector exposure to the international environment.

The assets of the banking sector continued to account for the lion's share of total assets of the financial system as at end December 2020 (79.24 percent), and the year ended with solid financial performance as evidenced by key financial soundness indicators. The banking sector remained adequately capitalized, liquid and profitable. However, the ratio of gross loans to total deposits remained very low (21.84 percent), the cost of financial intermediation remained high, with attendant impact for economic growth. Moreover, there was higher concentration of banking sector assets held in government securities, implying a greater tendency of crowding out credit to the private sector to finance investment and development. During 2020, bank lending was mainly channeled to the commerce & finance and miscellaneous sectors. However, commerce & finance and construction sectors accounted for the chunk of non-performing loans (NPLs), thus remaining a subject of intensive supervision. Taken together, there was increase share in lending to commerce & finance sector which has higher than average NPLs, conversely, there was a reduction in credit to construction which has a very high NPLs ratio and an increase to miscellaneous and business which are sectors with lower than average NPLs ratio.

The Bank recently introduced a number of guidelines and directives which are intended to ensure stability of the financial system. They include guidelines on Regulatory Sandbox Program; Rules for Administering the BSL Special Credit Facility for the COVID-19 Pandemic; Directives on Tiered KYC; Rules for administering BSL's Special Credit Facility; Monetary Policy Committees response to Economic impact of COVID-19; National Literacy Framework (2020-2024). Furthermore, the Bank adopted risk-based supervision, a Macro Prudential and Resolution Framework in line with international best practice. The establishment of Financial Policy Committee by BSL to oversee the maintenance of a stable financial system and to enhance coordination amongst key stakeholders in the financial sector is still in progress. Furthermore, the Financial Sector Stability Review (FSSR) Mission of the IMF was completed in 2020 and the report was presented in early 2021. Subsequently, the roadmap was discussed and is now waiting for its implementation which was put on hold due to COVID-19 pandemic. Also, the Financial Sector Assessment Program (FSAP) mission of the World Bank, which started in the first quarter of 2020 but slowed down due to COVID-19 pandemic, is expected to help address many of the financial sector challenges indicated in this report.

The BSL is confident and prepared to deal with the wide range of risks it could face so that the financial system can serve individual households and businesses even in the face of extremely difficult circumstances. The current state of financial stability, accompanied by the overall macroeconomic developments will result in further sustainable expansion of the financial system and its contribution to economic development. To safeguard the financial system stability of Sierra Leone, the BSL will continue to closely supervise and assess developments related to financial stability, invest in capacity building, and strengthen the financial system regulatory framework and infrastructure, while also increasing the frequency of its communication on financial stability issues.

Kelfala M. Kallon (Prof)

Governor

EXECUTIVE SUMMARY

The COVID-19 pandemic has caused a huge global economic crisis of unprecedented magnitude, which has triggered a global recession amid negative demand and supply shocks. Because of the pandemic, airlines were grounded, oil prices plunged, hotels shut down causing all forms of congregational economic activities to be halted. Global output contracted by 3.30 percent in 2020 but it is projected by the IMF to grow by 6.00 percent in 2021. This rebound is expected to be driven by continued expansionary fiscal policies and accommodative monetary policy stance.

Growth in advanced economies also receded to -4.60 percent in 2020 from 1.60 percent in 2019 but is projected by the IMF to rebound to 5.60 percent in 2021. Emerging and Developing Economies also witnessed a contraction of 2.10 percent in 2020 but growth is projected to rebound to an estimated 6.30 percent in 2021.

Real GDP growth in Sierra Leone was estimated at -2.20 percent in 2020 from 5.50 percent in 2019. The contraction was driven mainly by a decline in services, especially trade, travel and tourism, followed by agriculture industry and mining activities.

Notwithstanding the recession in 2020, total assets of the financial system increased by 30 percent rising to 42.14 percent of GDP. This increase mainly reflected the growth in assets of the commercial banks.

The banking sector in Sierra Leone continues to rely on government securities (largely 364-days T-bills) as the main source of income and almost one-half of total assets. This suggests there is excessive concentration risk in the banking sector. Another salient risk is the credit risk of lending to the private sector. That said, non-performing loans (NPLs) fell by one-quarter during 2020 to 12.7%. The decrease was driven by government payments to contractors, who in turn repaid bank loans.

The financial system was even more dominated by the banking sector, which accounted for 79.24 percent of the total financial system assets at end December 2020.

The banking sector's balance sheet grew by 37.67 percent, to Le13.10trn in 2020. The asset composition of the banking sector in 2020 shifted further to assets held with the government rather than private sector. A breakdown of assets shows that investments in government securities (Treasury Bills and Bonds) accounted for 44.28 percent followed by claims 27.68 percent and advances 15.71 percent compared to 43.37 percent, 23.38 percent and 19.01 percent in 2019 respectively. This reflects the preference banks have for holding relatively high yielding government securities with zero-risk weighting, which reduces the quantum of measured risk-weighted assets thereby improving both banks' capital base and profitability.

The Sierra Leone economy is projected by the IMF to grow by 3.0 percent in 2021, reflecting the assuaging impact of the COVID-19 pandemic, given the administration of vaccines (with 192,000 doses of AstraZeneca vaccines already rolled-out in 2021 via the Covax Facility) and full resumption of economic activity in the key sectors of the economy. Sierra Leone GDP growth is expected to increase further in 2022 to 3.6 percent, driven by the fiscal, monetary and structural measures put in place by the government, likely extension of BSL Special Credit Facility, and resumption of iron-ore mining.

The financial system remains sound and stable, as reflected in the positive trend in most of the key Financial Soundness Indicators. Financial soundness indicators suggest that most banks remain highly capitalised and liquid with cushions well above regulatory minimal. NPLs fell despite an increase in the share of credit to the relatively risky [i.e. higher than average NPL rates] commerce and finance sector. This may be attributed to an increase in credit share to the relatively safe miscellaneous and business sectors and fall in a credit share to the very risky construction sector. And most banks passed a barrage of stress tests to private sector loans and banks' liquidity since a large part of banks' assets are held with government and these are assumed risk free and highly liquid.

In addition, BSL continued with its effort to strengthen the regulatory and supervisory framework for the financial system in 2020. Accordingly, BSL issued additional measures to combat the unlawful trading in foreign currency to strengthen financial sector stability. Moreover, the Bank issued Guidelines on Regulatory Sandbox Program; Directives on Suspension of Payments of Dividends for Financial Years 2019 and 2020; Directives on Tiered KYC, Rules for Administering BSL's Special Credit Facility; National Financial Literacy Framework (2020-2024) and Guidelines on Use of Agents. Furthermore, the minimum paid-up capital has been increased from Le30.00bn to Le85.00bn over a three-year period effective December, 2019. As at end December 2019 banks were required to increase their minimum paid-up capital from Le30billion to Le45 billion, to Le65billion as at end December, 2020 and to Le85billion by end December 2021. This was done to improve banks' capacity to absorb losses and be more resilient to potential shocks that would emanate from their operations.

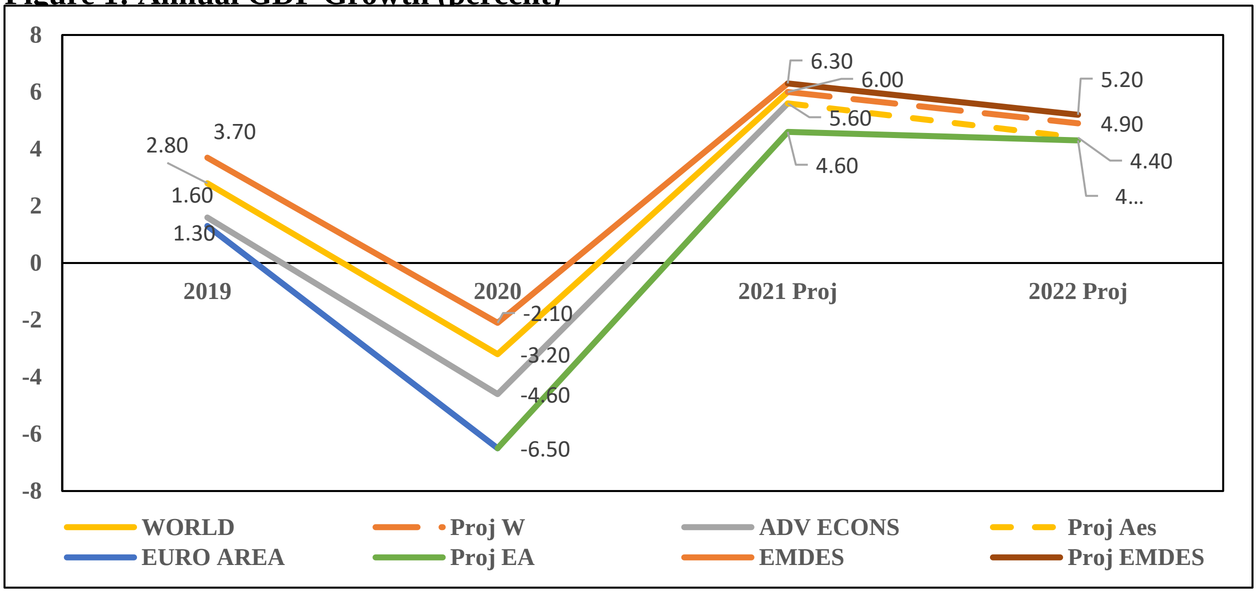
CHAPTER ONE

1.0 GLOBAL MACROECONOMIC AND FINANCIAL DEVELOPMENTS

1.1 Global Macroeconomic Developments

The COVID-19 pandemic has caused a global economic crisis of unprecedented magnitude, which triggered a global recession amid negative demand and supply shocks. As airlines were grounded, oil prices plunged and hotels shut down, causing all forms of congregational economic activities to be halted. According to John Hopkins University, global COVID-19 pandemic cases reportedly amounted to 73.60 million as at 16th December, 2020, this include over 1.60 million deaths and 41.70 million recoveries. These developments in part led to contraction in global output growth to -3.20 percent in 2020 from 2.80 percent in 2019. A rebound to 6.00 percent is however projected for 2021. This rebound is driven by expansionary fiscal policies and accommodative monetary policies to ease the effects of COVID-19 pandemic. Growth in advanced economies receded to -4.60 percent in 2020 from 1.60 percent in 2019 but is projected –by the IMF to rebound to 5.60 percent in 2021. Furthermore, growth in the Euro Area contracted by -6.50 percent in 2020 from 1.30 percent in 2019 but is projected to increase to 4.60 percent in 2021. Emerging markets and developing economies also recorded a contraction of -2.10 percent in 2020 from 3.70 percent in 2019 though GDP growth is projected to rebound to an estimated 6.30 percent in 2021.

Figure 1: Annual GDP Growth (percent)



Source: IMF WEO July, 2021

Output losses have been particularly large for countries that rely on tourism and – initially at least – commodity exports and for those with limited policy space to respond. Many of these countries entered the crisis in a precarious fiscal situation and with less capacity to mount major health care policy responses or support to livelihoods.

Future economic developments will depend significantly on the path of the health crisis, including whether the new COVID-19 strains prove susceptible to vaccines or they prolong the pandemic; the effectiveness of policy actions to limit persistent economic damage; the evolution of financial conditions and commodity prices; and the adjustment capacity of the economy. In many aspects, this crisis is unique. In certain countries, policy support and lack of spending opportunities have led to large increases in savings that could be unleashed very quickly should uncertainty dissipate. At the same time, it is unclear how much of these savings will be spent, given the deterioration of many firms' and households' balance sheets (particularly among those with a high propensity to consume out of income) and the expiration of loan repayment moratoria. In summary, risks are assessed as balanced in the short term, but tilted to the upside later on. Policymakers should prioritize policies that would be prudent, regardless of the state of the world that prevails.

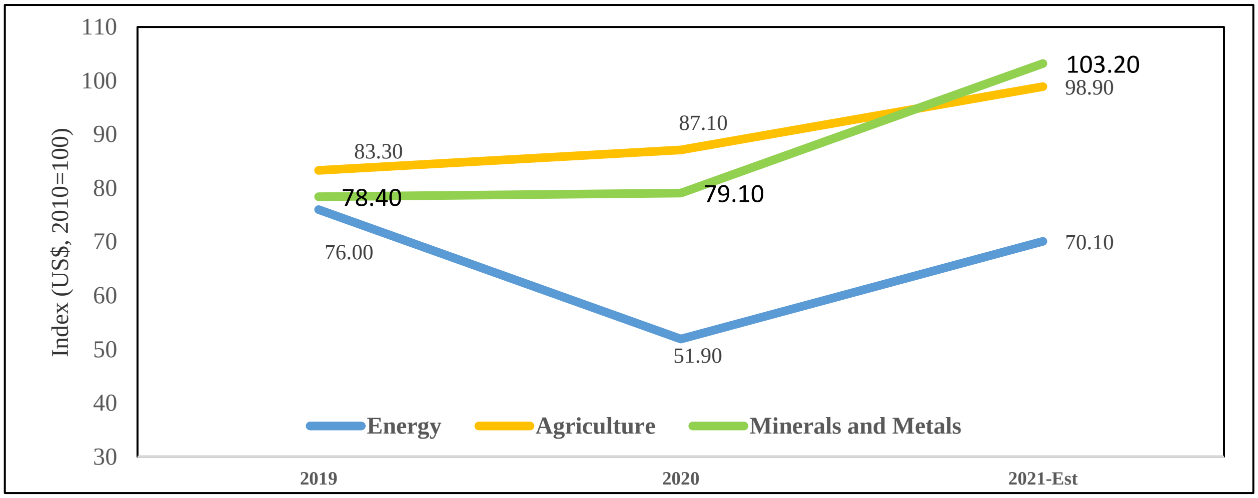
1.2 Recent Developments in Commodity Prices

Agriculture commodities price index rose by 4.36 percent in 2020 and it is projected to further increase to 98.90 in 2021. The Price Index for Minerals and Metals saw a marginal increase by

0.89 percent in 2020 and projected to increase to 103.20 in 2021. On the other hand, Energy saw a huge decrease by 31.71 percent in 2020 and projected to increase to 70.10 percent in 2021. The gradual pick-up of metal prices in response to a faster-than-expected pick up in China's industrial activities is expected to provide some reprieve in 2021.

Looking ahead, oil prices are forecast by the World Bank to average $56/bbl in 2021, more than one-third higher, on average, than in 2020, and see a further small rise to $60/bbl in 2022 as global demand continues to gradually rise. Metal prices are expected to average 30 percent higher in 2021 than in 2020 due to strong demand, before dropping back somewhat in 2022. Agriculture prices are forecast to average nearly 14 percent higher in 2021, driven by a few food commodities, and are expected to stabilize thereafter. The main risks to the price forecasts are the evolution of the pandemic for industrial commodities, and weather shocks for agriculture.

Figure 2: Commodity Price Indices



Source: WB Commodity Market Outlook April, 2021

1.3 Global Financial Developments

Despite the fact that the global financial markets in 2020 were largely buoyant, fiscal and monetary measures bolstered liquidity and triggered a sentiment for stocks amid low yields on bonds as major indices around the world returned positive. They include Morgan Stanley Capital International (MSCI) emerging market index (+15.80percent), the Dow Jones Industrial Average (+7.30percent), S&P 500 (16.30percent), Tech-Heavy Nasdaq (+43.60percent) amongst others all gained despite the COVID-19 pandemic.

As a result of the COVID-19 pandemic, central banks around the world have pursued highly expansionary monetary policies to ease financial conditions in order to maintain the flow of credit to households and firms thereby supporting aggregate demand. Liquidity needs by firms and households have been met by additional debt, which has for the time cushioned the devastating effects of the COVID-19 pandemic. More specifically, financial markets have shrugged off the most recent softening in economic activity. Regardless of persistent uncertainties surrounding the economic outlook, investors appear to remain confident about growth prospects in 2021, expecting that continued policy support will offset any possible near-term disappointment. The disconnect between financial markets and the real economy, however, persists. Despite the recent rise in US long-end rates, market participants point to expectations of very low rates over the coming years and upward revisions in earnings expectations since the vaccine announcements serve as justification for the market rally.

Vaccine access is likely to remain uneven across countries, and equitable distribution may take time. Many high income economies, such as Canada, some European Union countries, the United Kingdom, and the United States, have pre purchased vaccines. By contrast, procurement of vaccine doses for emerging market and developing economies via direct negotiation or through the multilateral COVAX pillar lag significantly. The need for access to vaccines is particularly urgent in countries where cases have accelerated recently or remain very high.

The prospect for global stocks in 2021 remains positive given the reopening of economies, the rebound in household spending and the demand outlook for household expenditure. Even though, it is expected that government fiscal programs and interventions will be reduced in 2021, an accommodating monetary stance expected to be sustained throughout 2021 continues to brighten the outlook for stocks.

Policymakers are expected to remain vigilant to the risks of high leverage, designing policies to deal with highly indebted firms, increased supervisory attention to risk taking and will likely be swift to implement macro prudential tightening as and when macroeconomic conditions permit.

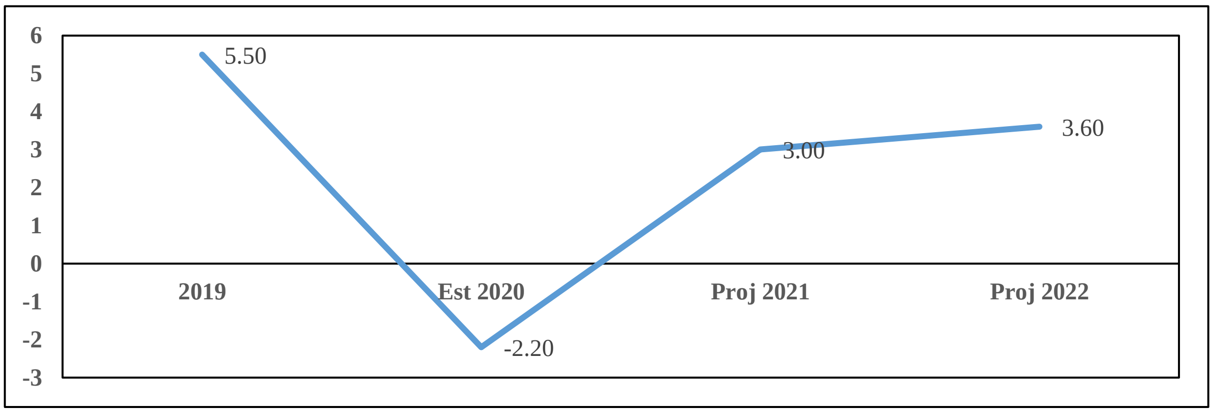
CHAPTER TWO

2.0 DOMESTIC MACROECONOMIC DEVELOPMENTS

2.1 GDP Growth and Inflation

Real GDP in Sierra Leone was estimated to have decline by 2.2 percent in 2020 following an increase of 5.50 percent in 2019. This was due to the COVID-19 pandemic in 2020 with its attendant effects on trade, investments and outputs.

Figure 3a: Real GDP Growth Rate in Sierra Leone (2019- Projected 2022)



Source: MEFT, IMF Rapid Credit Facility, January 2021

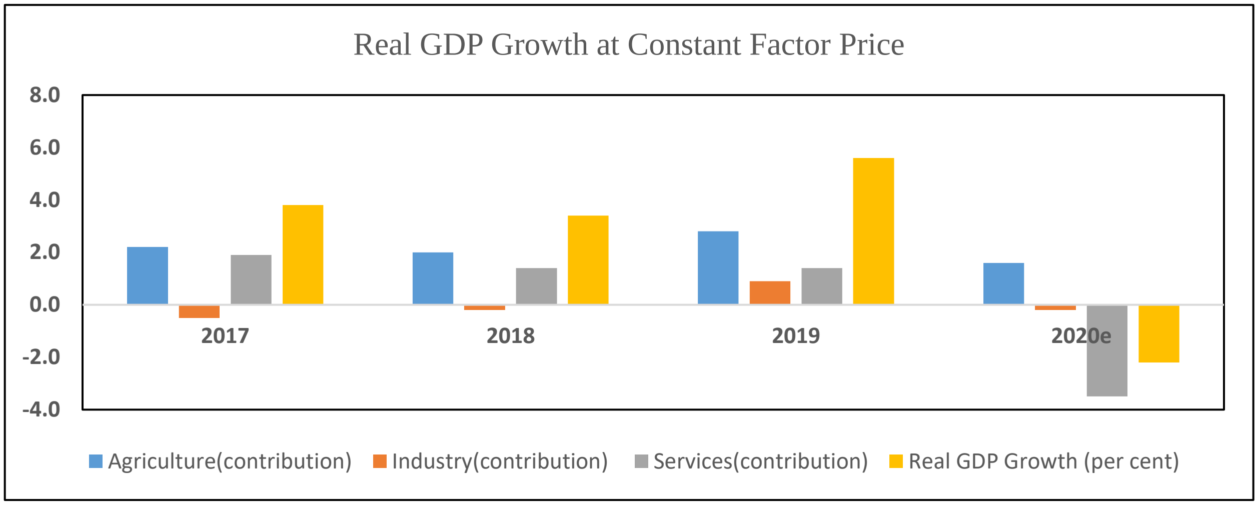
The contraction was concentrated especially in services, particularly trade, travel and tourism and, to a lesser extent, in agriculture and mining activities.

Table 1: Real GDP Growth, at Constant Factor Price

Sectors	2017	2018	2019	2020e
Agriculture(contribution)	2.2	2.0	2.8	1.6
Industry(contribution)	-0.5	-0.2	0.9	-0.2
Services(contribution)	1.9	1.4	1.4	-3.5
Real GDP Growth (percent)	3.8	3.4	5.6	-2.2
Average Sectoral Growth	1.2	1.1	1.7	-0.7

e= estimate- Source: World Bank Group, Sierra Leone 2021 Economic Update

Figure 3b: Real GDP Growth rate (2019- Estimated 2020)



Source: World Bank Group, Sierra Leone 2021 Economic Update

The inflation rate fell in the year to end 2020 from 14.8% to 13.50 percent below BSL' target (17.50 percent). The main driver was a decline in non-food inflation. The inflation rate is expected to increase in 2021 with end December projected by the IMF at 13.30 percent.

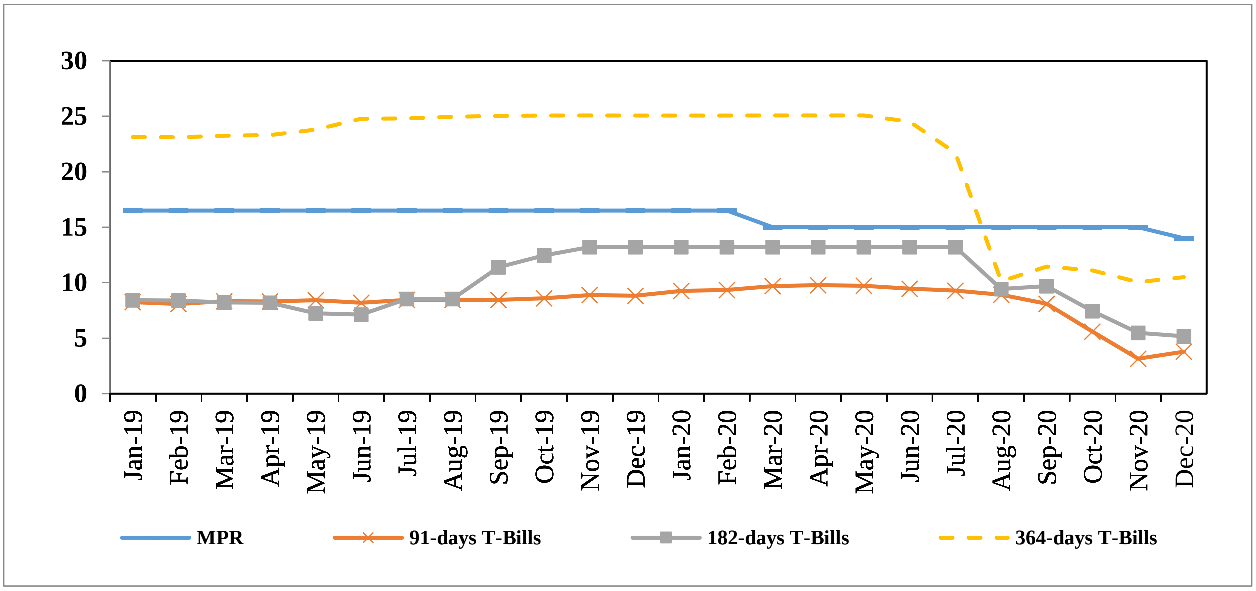
2.2 External Sector

The current deficit narrowed to 15 percent of GDP from 22.3 percent of GDP in 2019 aided by improvement in trade deficit and current transfers. The reduction in merchandise imports counterbalanced the decline in exports causing the trade deficit to narrow to 2.6 percentage points of GDP while increased support by development partners increased official transfers by 2.8 percent points to 8.4 percent of GDP ($353.4mn). The net inflow to the capital and financial account helped finance the current account deficit although it fell by 5.9 percentage point to 9.1 percent of GDP (US$384.5mn) in 2020 due mainly to adverse impact of Covid-19 Pandemic on the mining sector, worsened by the arbitration between Government and SL Mining Company Limited. Gross International Reserves increased from 3.8 months of import(US$507mn) in 2019 to 4.7 months of imports(US$677mn) reflecting increased budgetary and balance of payment support from development partners(including International Monetary Fund and World Bank). The Leone was relatively stable against the US dollar; depreciating by 4.4 percent (year –on-year) in 2020 relative to 15.3 percent in 2019. Exchange rate stability was supported by BSL's intervention to facilitate the importation of essential commodities (food and fuel) as well as administrative measures to limit uncertainty and prevent speculative pressures to destabilize the already thin market. However, the IMF (2020) estimates the Sierra Leone's real effective exchange rate to be overvalued by around 20-30 percent consistent with historic high current account deficits and reflecting the considerable appreciation of the Leone.

2.3 Monetary Policy Management

The monetary policy stance was loosened in 2020 with the monetary policy rate (MPR) cut twice, in March and in November 2020 as a means of spurring economic growth and providing reprieve to Small and Medium Size Enterprises (SMEs) and other businesses that were hurt by the COVID-19 Pandemic. The big fall in the 364-day treasury bills in mid-2020 was driven by the reduction in government borrowing appetite, as budgetary and balance of payment support from development partners was received by the Government of Sierra Leone. This reduced borrowing fed through to reduce the yields in the 364-day tenor as shown in Figure 4

Figure 4: Monetary Policy and T-bill Rates



Source: Research, BSL

CHAPTER THREE

3.0 SYSTEMIC RISKS ASSESSMENT

3.1.1 Stress Test Analysis

Stress tests are forward-looking exercises that aim to evaluate the impact of severe but plausible adverse scenarios on the resilience of banks and the banking system as a whole. The capital adequacy ratio (CAR) is the main indicator used in BSL's model to verify the adequacy of the strength of banks' balance sheets. BSL has set the statutory CAR for banks operating in Sierra Leone at 15 percent, which is almost twice as high as the international minimum standard of 8 percent set by the Basel Committee. The higher ratio applied by BSL is a prudent approach aimed at providing banks with an additional buffer against potential shocks. Two of the banks in the sample fail to meet this prudential threshold currently.

The stress test analysis for end December 2020 covered fourteen banks in Sierra Leone to assess their resilience to shocks to credit, liquidity, foreign exchange and interest rate risks. The stress test analysis was complemented by reverse stress test and scenario based multi-factor stress tests.

The credit risk stress tests are split into various types including migration from performing to non-performing loans, across different specific loan categories (substandard, doubtful, loss loans), proportionate increase in NPLs, sectoral shocks to NPLs, and large exposures. BSL's in-house model is first used to determine 50 percent migration across the different loan categories before fully employing the IMF's Cihak Model. This IMF's Cihak stress testing model is used to verify whether the banking system can withstand different levels of economic shocks. The scenarios are built based on assumptions, using future potential shocks, at the same time considering past events that may disrupt the financial system, either in part or holistically.

The stress test also assessed the foreign exchange risk under a baseline and adverse scenarios for the Leone exchange rate. Contagion risk was assessed based on the size of banks' interconnectedness and exposures via inter-bank placements and takings. This risk gauges the likelihood that banks will be unable to meet their debt obligations between themselves. Interest rate risk measures the impact of an adverse movement in interest rate on banks' capital. In this context the focus is on 364-day t-bills rate. Fourth, liquidity risk which is the likelihood that banks will not be able to meet their short term obligations, was also assessed by the stress test.

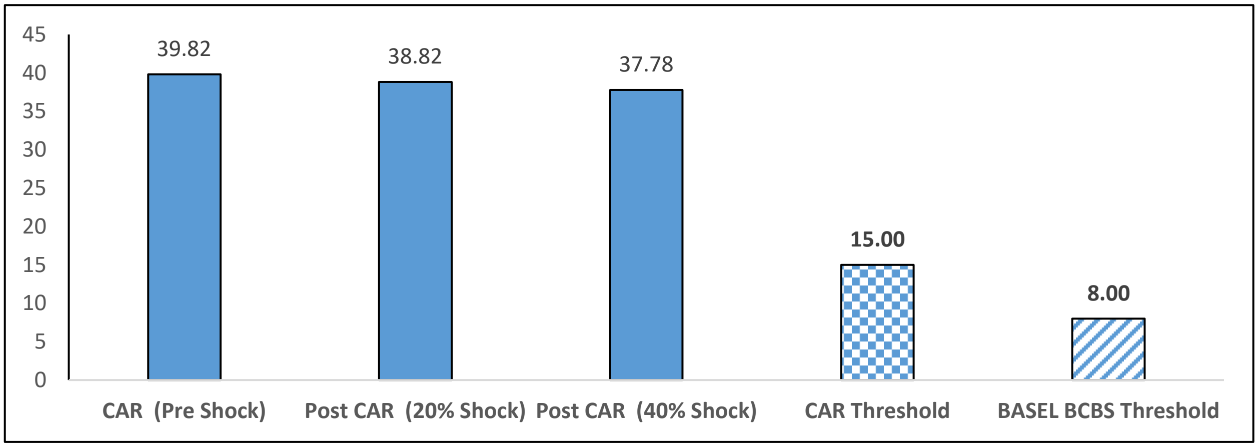
Finally, a stress scenario attempting to measure the Covid-19 shock was included in the suite of stress tests.

3.1.2 Credit Risk

Scenario on Credit Migration

Stress tests on credit shocks were run to determine the effect on banks' capital emanating from further deterioration in asset quality. The first stress test on credit risk employs the Bank's simplified in-house model and assesses the impact of 30 and 50 percent migration across various loan categories. The first scenario assumes a migration of 50 percent across the various NPLs categories; doubtful to loss then substandard to doubtful. The second scenario assumes migration of 30 percent from the current loan category to the substandard category. The intuition behind this scenario is driven by the fact that experience from on-site examination shows that banks most times do not properly classified their loan books thereby understating their NPLs and subsequently under provision and so overstate their capital position. The 20 percent and 40 percent shock reflect the effect of increased NPLs and how they feed through to impact the capital of banking sector.

Figure 5a: Results of Credit Migration in the Banking Sector Across Various Categories of Loans (BSL in-house model)



Source: FSD, BSL

The results indicate that the banking sector as a whole remains resilient post migration with CARs falling only modestly in both the 20% and 40% shock cases (Figure 5a). Also, no additional individual banks fail to meet the CAR threshold of 15 percent.

For the shock on proportional increase in NPLs, the stress test revealed that the banking sector could withstand a shock of up to 125.00 percent increase in the industry's existing NPLs for the banking sector CAR to remain, on average, above the 15.00 percent regulatory prudential limit.

The assumptions underscoring the stress test on proportional increase in NPLs are scenarios of a 50, 100, and 125 percent increase in NPLs, with existing performing loans. This scenario would arise if customers were somehow unable to pay off their current existing credit facilities with the banks. Accordingly, the rise in NPLs would require a very severe shock. The intention behind analyzing such a scenario is to better understand how resilient the banking sector is to such severe shocks. The outcomes are shown in Table 2.

Table 2: Stress Test Results of Proportional Increases in NPLs

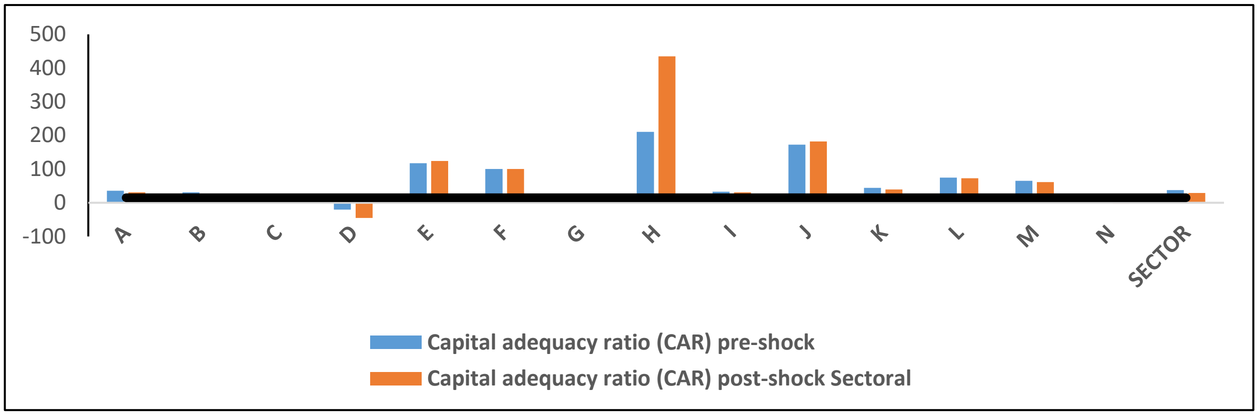
Credit Default Shocks scenario	Solvency Ratio aftershocks Banking Sector	Number of banks below CAR Regulatory Threshold
Current NPLs	37.9	2
50 percent NPLs increase	29.6	3
100 percent NPLs increase	20.5	4
125 percent NPLs increase	15.0	5
126 percent NPLs increase	14.8	5

Source: FSD, BSL

3.1.3 Sectorial Increase in NPLs

A more granular approach to increases in NPLs was considered to assess the impact on specific sectors. Sectoral credit concentration risk is assessed via sector wide shock to NPLs which assumes NPL rate rises by sector to 70 percent for commerce and finance (reflecting cyclicality), 50 percent for mining and quarrying, construction and other trade and tourism, 30 percent for communication and 25 percent for all other sectors. The sectors were chosen due to their engagement within the domestic economy reinforcing cyclicality across these sectors. The results demonstrate that the banking sector as a whole can withstand such a differentiated proportional increase to NPLs with the CAR after the shock at 29.3 percent. At the individual level, only one additional bank fails to meet the regulatory CAR threshold. This is illustrated also in Figure 5b.

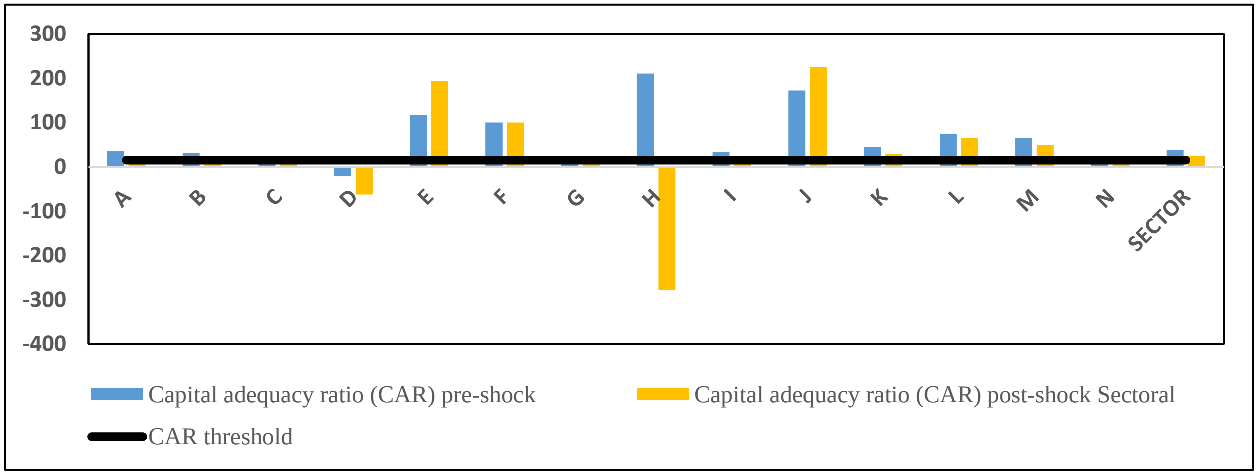
Figure 5b: Results of Sectoral Shocks to NPLs



Source: FSD, BSL

Another plausible scenario is the assumption that the five largest exposures of the banking sector as a whole will become NPLs, and the provisioning rate is 100 percent. This could have a more severe impact on the banking sector's capital. Nonetheless, at 24.3 percent, the industry CAR is found to remain well above the prudential minimum. The impact of the various credit risk scenarios on individual banks is shown in Figure 5c.

Figure 5c: Results of the Five Large Exposures of the Banking Sector Becoming NPLs



Source: FSD, BSL

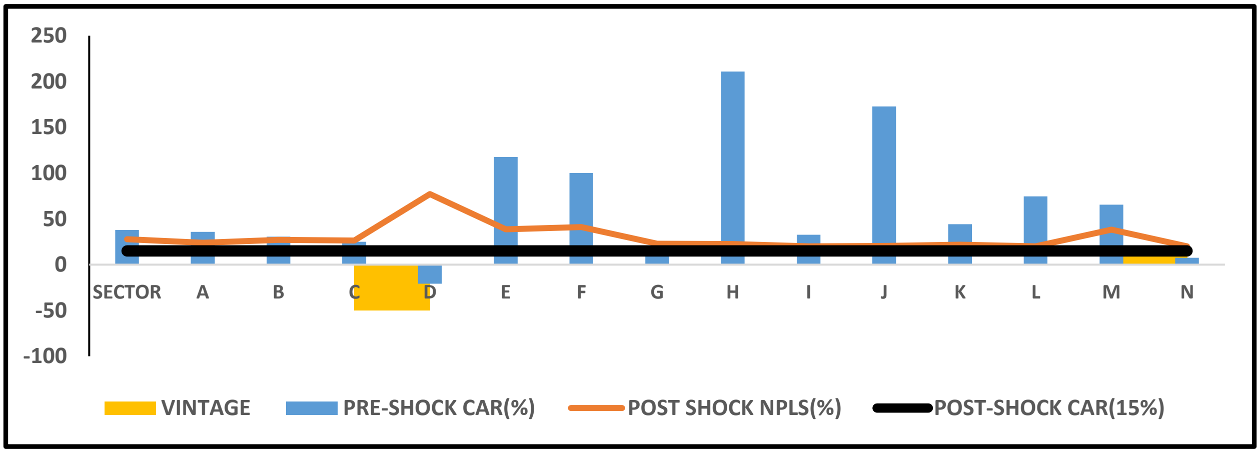
3.1.4 Reverse Stress Test

The reverse stress test determines by how much does NPLs need to deteriorate for the banking sector-wide CAR to fall below the 15 percent regulatory threshold. The assumptions are that in case provisioning for additional NPLs increase by 40 percent and the impact on RWA on Capital (percent) is 100 percent. This means that by how much NPLs needs to increase to reduce CAR below the 15 percent regulatory threshold which is illustrated in figure 6

The result shows that the banking sector is resilient post shock of 40 percent additional provisioning emanating from an implied increase in NPLs of 80 percent. However, two banks were below the threshold CAR pre-shock. It is important to note that the chart shows the result of post shock NPLs dynamics for each bank and the banking sector.

It is worth noting however that the reverse stress test result in figure 6 is different from the result in Table 2. Table 2 illustrates the result of a proportional increase in NPLs whiles figure 6 illustrate the results using the reverse stress test scenario and how both of them impact on the CAR.

Figure 6: Increase in NPLs Needed to Reduce Individual Nanks' CARs to the Regulatory Minimum



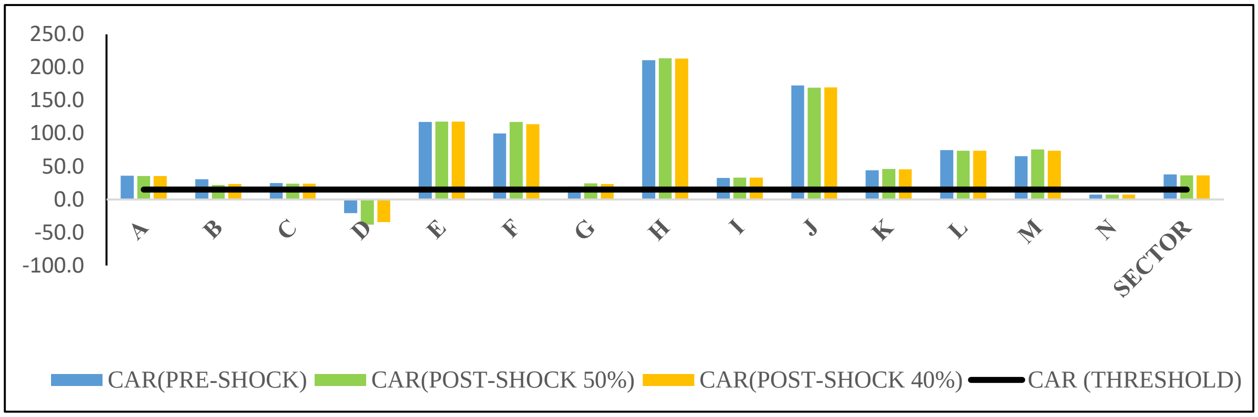
Source: FSD, BSL

Banks should, in practice, be proactively managing their portfolio given the severe impact of the increasing NPLs.

3.1.5 Foreign Exchange Risk

The direct foreign exchange scenarios assume that the Leone depreciates by 40 and 50 percent, respectively. This though only has a very small impact on most banks' capital adequacy ratios (Figure 7). The main point from this exercise is that there is little net impact on the banking sector as a whole but for some banks capital rises and for some it falls depending whether they have net foreign assets or liabilities.

Figure 7: Result of Direct Forex Shocks

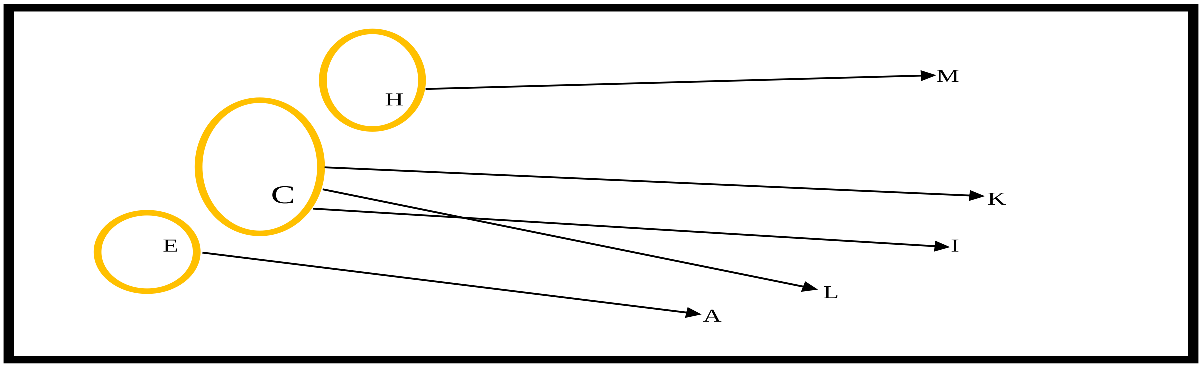


Source: FSD, BSL

3.1.6 Interbank Stress Test (Contagion Risk)

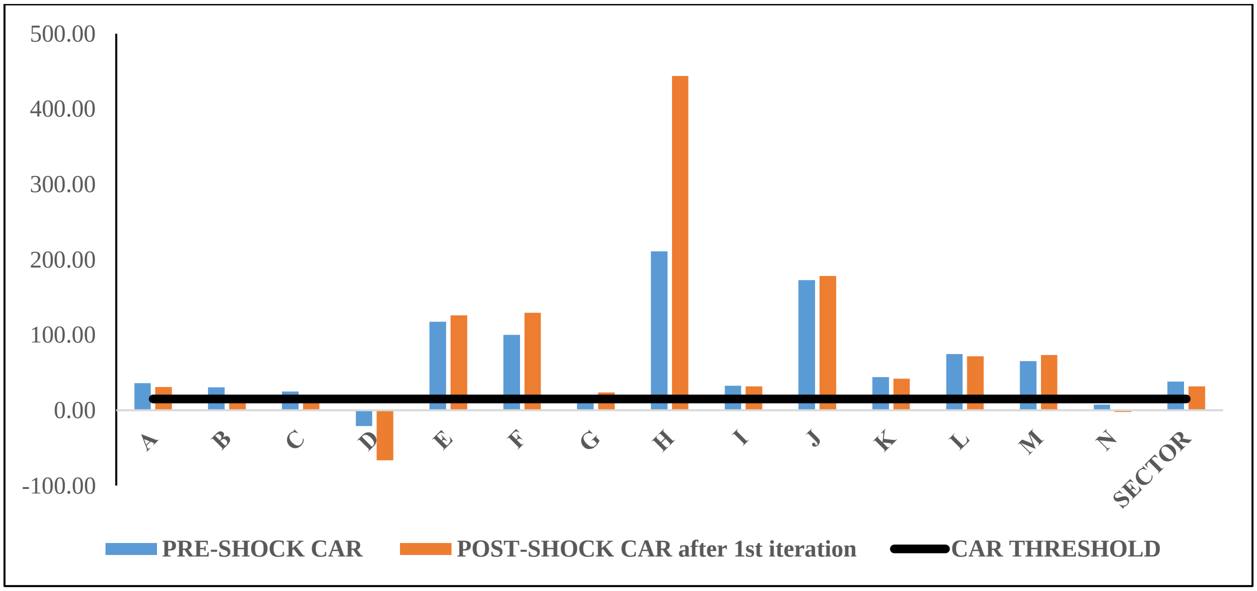
Contagion risk, which arise as a result of the degree of interconnectedness of banks through interbank placement and takings, increased over the review period. One bank was most central to the network as it was exposed to at least two counterparties during the year. As at end December 2020, three banks have an outstanding placements amounting to Le88 billion, whilst four banks have outstanding takings amounting to Le88 billion. Of the total outstanding takings, one bank accounted for 47.2 percent, whilst one bank accounted for 35.8 percent the total outstanding placements as at end December, 2020. The value of interbank transaction in 2020 was over Le3 trillion and one non-bank financial institution serving as a significant player in the interbank market. This shows the level of interconnection of the financial system. These networks or lines in figure 8a indicate the direction of lending in terms of lenders and borrowers. The underpinned assumption for the interbank stress test was impacted at 20 percent of risk weighted assets on capital.

Figure 8a: Network Analysis Based on Interbank (Anonymized) Exposures as at December 2020



Note: Node color representation (Orange= Lenders; Nodeless= Borrowers); the sizes of the nodes represent the quantum of transactions over the coverage period.

Figure 8b: Results of Inter-Bank Stress Test



Source: FSD, BSL

The scenario on interbank stress test assessed the shock that the borrowers of funds were unable to repay the lenders of funds. Although the interbank stress test only had a modest impact in reducing the CAR of the system as a whole, the CAR for two additional banks fell below the regulatory threshold (Figure 8b).

3.1.7 Liquidity Risk

The liquidity stress test results determined the liquidity status of the sector in an unfavourable economic condition, testing the impact on a bank's ability to meet its short term obligations. This may occur from a sizeable deposit withdrawal from a Domestic Systemically Important Bank (D-SIB) or from all banks.

Commercial banks in Sierra Leone are subject to prudential minimum liquidity ratio of 40 percent for demand deposits and 20 percent for savings and time deposits. Most banks have liquidity ratios well above these regulatory minimum requirements. The scenario assessed the impact of a 20 percent daily withdrawal of demand deposits for five consecutive days from all banks simultaneously. This assumes that customers do not switch deposits from one bank to another but rather reduce deposits from all domestic banks. The impact of this simple liquidity stress test indicated that all banks can withstand such a liquidity shock (Table 3).

Table 3: Simple liquidity stress test results

Shock: 20 percent daily withdrawal of deposits for five days	Post Shock: Number of illiquid banks
After day 1	0
After day 2	0
After day 3	0
After day 4	0
After day 5	0

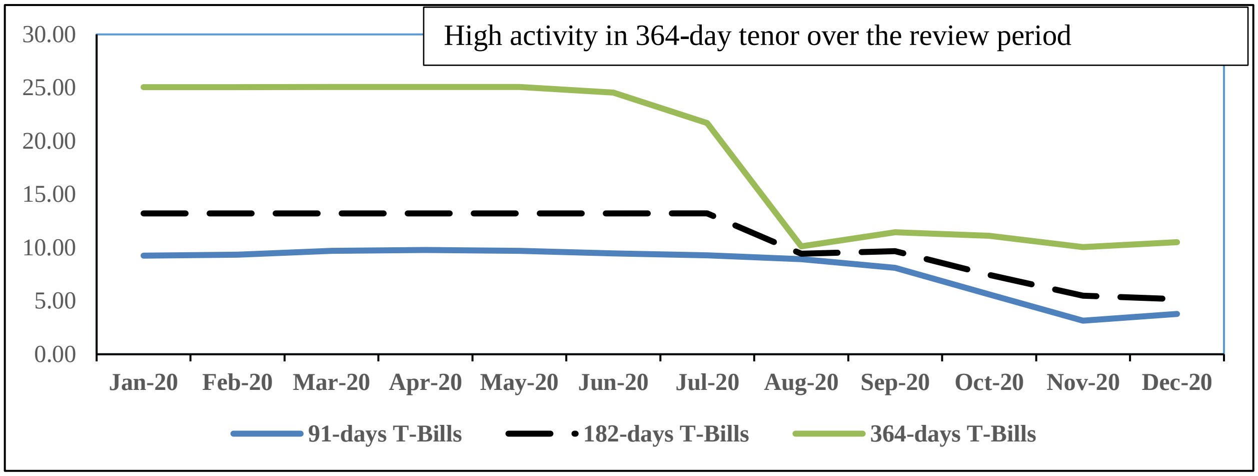
Source: FSD, BSL

This result is because initial liquidity ratios are so high (and much above min thresholds) – which in turn reinforces the fact that banks' government treasury bills holdings are highly liquid assets.

3.1.8 Interest Rate Risk

The scenario of the interest rate shock on government securities was run using average weighted interest rate of the 364-day T-bills, because most investors/commercial banks lock their funds into this tenor due to their relatively attractive returns (Figure 9a). The actual shock deployed is the 40 percent shock to the 364-day tenor and this transmits to the CAR.

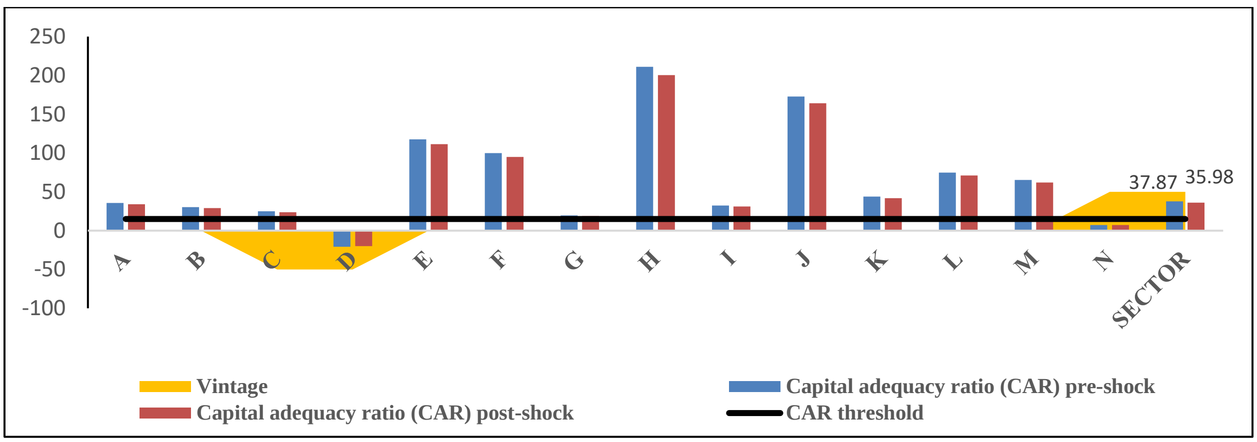
Figure 9a: Dynamics of T-bills Yields over the Period 2020



Source: Research Department, BSL

The CAR of the banking sector as a whole and of individual banks fell only marginally as a result of this interest rate shock (Figure 9b). It is important to note that the shock marginally affected the two banks that were already in red with regards to their capital.

Figure 9b: Results of Interest Rate Shock



Source: FSD, BSL

In conclusion, it would take a very big shock to banks risks for CAR to fall below 15% CAR and liquidity ratio to fall to min thresholds partly for positive reasons because - most banks start with high CAR and liquidity ratios well about regulatory threshold but also reflects for credit risk that it would take a big shock to have much impact in reducing CAR since bank loans only account for 17.34 % of the banks total assets.

CHAPTER FOUR

4.0 FINANCIAL SYSTEM DEVELOPMENTS

4.1 Structure of the Financial System

The financial system remains dominated by the banking sector accounting for 79.24 percent of total financial system assets as at end December 2020. The pension fund ranked second with 14.25 percentage share followed by the insurance and the deposit taking microfinance sectors, which accounted for 2.10 percent and 2.09 percent respectively and others accounting for the rest.

The number of regulated financial institutions by the Bank of Sierra Leone increased to 251 from 214 in 2019. The number of commercial banks remained at 14, DTMFIs at four (4), Community banks seventeen (17), FSAs 59 and stock exchange at one (1). On the other hand, COMFIs increased to 41 in 2020 from 28 in 2019, Foreign Exchange Bureaux to 96 in 2020 from 73 in 2019 and mobile money service providers to 3 in 2020 from 2 in 2019. The number of insurance companies regulated by SLICOM remained at 12 while pension fund (NASSIT) remained at one.

4.2. Total Assets of the Financial System

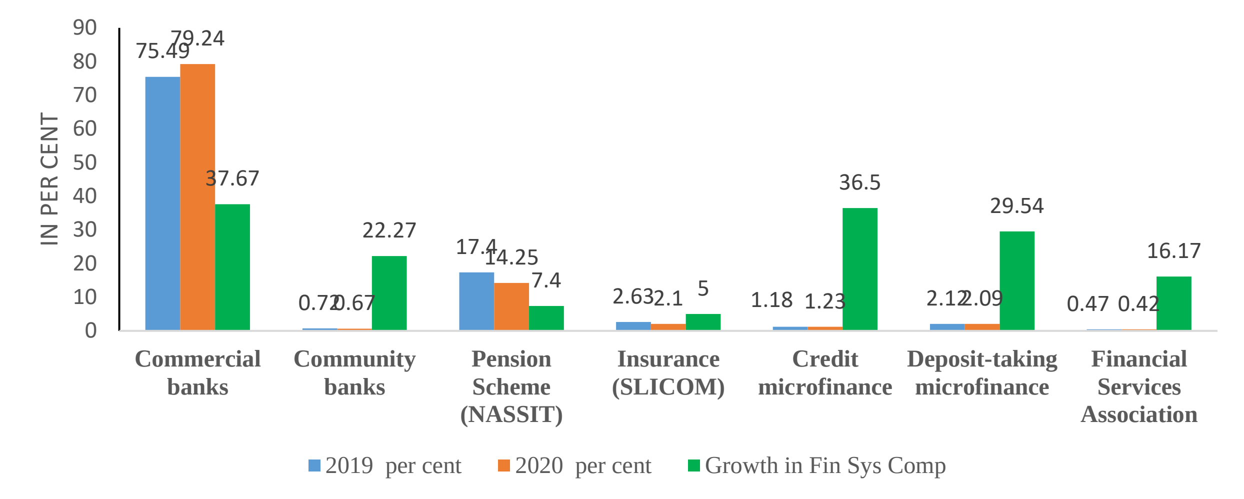
Total assets of the financial system increased by 31.15 percent to Le16,501.06bn in 2020 from Le12,582. 25bn in December 2019 representing 43.24 percent of GDP. The increase was mainly as a result of growth registered in the assets of all component of the financial system. The banking sector remained the dominant player and accounted for 79.24 percent followed by the pension fund (NASSIT) with 14.25 percent share.

Table 4: Composition of Assets in the Financial System

Financial System Components	2019 percent	2020 percent	Growth
Commercial banks	75.49	79.24	37.67
Community banks	0.72	0.67	22.27
Pension Scheme (NASSIT)	17.40	14.25	7.40
Insurance (SLICOM)	2.63	2.10	5.00
Credit microfinance	1.18	1.23	36.50
Deposit-taking microfinance	2.12	2.09	29.54
Financial Services Association	0.47	0.42	16.17
Total	**100.00**	**100.00**	**31.15**

Source: FSD, BSL

Figure 10: Composition of Assets in the Financial System, 2019 & 2020



Source: FSD, BSL

4.3 Banking Sector Performance

The banking sector consists of fourteen commercial banks – two state-owned, two domestic privately-owned and ten foreign-owned subsidiaries mainly from Nigeria, all regulated under the Banking Act, 2019. The banking sector's balance sheet grew by 37.67 percent, to Le13.10trn in 2020 from Le9.5trn in 2019. A breakdown of assets shows that investments in government securities (Treasury Bills and Bonds) accounted for 44.28 percent followed by claims 27.68 percent and advances 15.71 percent compared to 43.37 percent, 23.38 percent and 19.01 percent in 2019 respectively. This reflects the preference over the years for higher holdings of government securities with a zero-risk weighting, which reduces the quantum of risky assets that improves banks capital base.

Table 5: Assets Composition in the Banking Sector 2019-2020

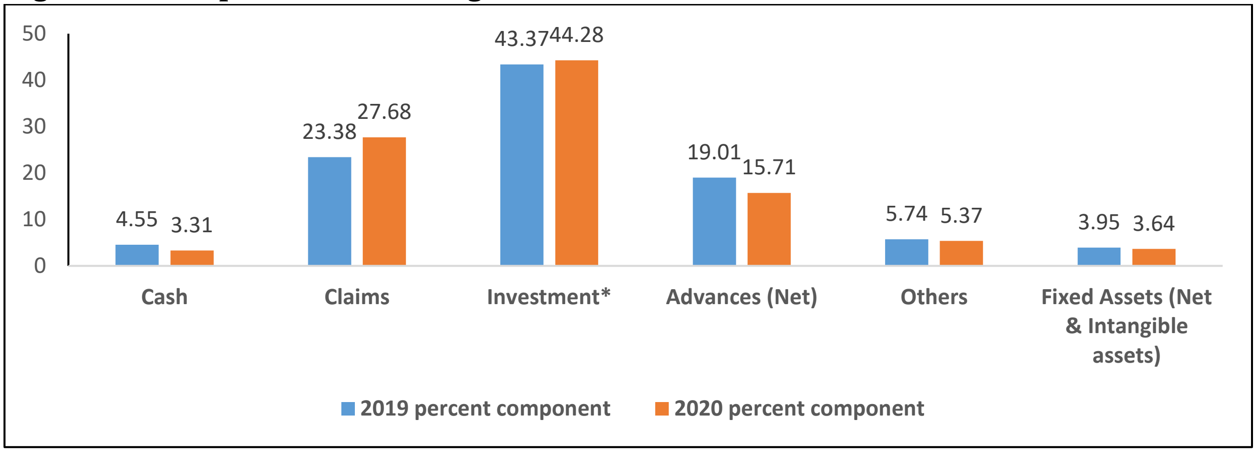
Banking Sector	**2019 (Le 'bn)**	**Percent Component**	**2020 (Le 'bn)**	**Percent Component**	**Percent Growth in 2020**
Cash	432.61	4.55	432.52	3.31	-0.02
Claims	2,220.82	23.38	3,619.92	27.68	63.00
Investment*	4,118.88	43.37	5,790.47	44.28	40.58
Advances (Net)	1,806.02	19.01	2,054.69	15.71	13.77
Others	544.82	5.74	701.77	5.37	28.81
Fixed Assets (Net) & Intangible assets	374.75	3.95	476.28	3.64	27.09
Total Assets	**9,497.90**	**100**	**13,075.65**	**100**	**37.67**

Source FSD Investment*: mainly government securities

Claims grew 63 percent in 2020 and include funds placed by commercial banks in BSL, Foreign-Resident, Foreign-Non Resident, Local Banks, Foreign Banks, Interbank Placement and Placement with Discount Houses.

Bank assets grew rapidly in 2020. This was mainly attributable to the need to finance government measure to support the real economy in face of the COVID-19 shock. But this has increased the banking sectors concentration risk and meant that credit to the private sector remains at very low levels(both absolute and relative to the size of the Sierra Leone economy).

Figure 11: Composition of banking sector assets 2019-2020



Source: FSD, BSL

4.3.1 Financial Soundness Indicators

The banking sector, which makes up the lion share of assets and deposits in the Sierra Leone's financial system, continued to expand (assets relative to nominal GDP) and remained adequately capitalised, liquid and profitable. Regulatory capital to risk weighted asset (capital adequacy) was 39.82 percent in 2020, down slightly from 2019 level of 41.73 percent. Asset quality seemed to improve, as the ratio of non-performing loans to total loans dropped to 12.67 percent from 16.83 percent in 2019. Return on asset (ROE) and return on equity (ROE) were 6.11 percent and 26.65 percent respectively similar to 2019 levels while measured liquidity in the banking sector was adequate as all indicators recorded increases from levels that were already well above regulatory minima (Table 6)

Table 6: Financial soundness indicators, 2019-2020

INDICATORS	Dec.2019	Dec.2020
CAPITAL ADEQUACY	**percent**	**percent**
Regulatory Capital to risk-weighted assets (percent)	41.73	39.82
Primary capital to risk-weighted assets (percent)	33.91	33.15
ASSET QUALITY AND COMPOSITION		
Nonperforming loans to total gross loans	16.83	12.17
Nonperforming loans net of provisions to capital	7.22	4.32
PROFITABILITY AND EFFICIENCY		
Return on Assets	6.12	6.11
Return on Equity	26.08	26.65
Interest margin to gross income	66.86	69.99
LIQUIDITY		
Cash ratio	17.72	20.74
Liquid assets to total assets	68.37	73.39
Liquid assets to short-term liabilities	86.84	89.64
Overall liquidity	107.97	109.17
SENSITIVITY TO MARKET RISKS		
Net open position in foreign exchange to capital	-1.75	-7.49

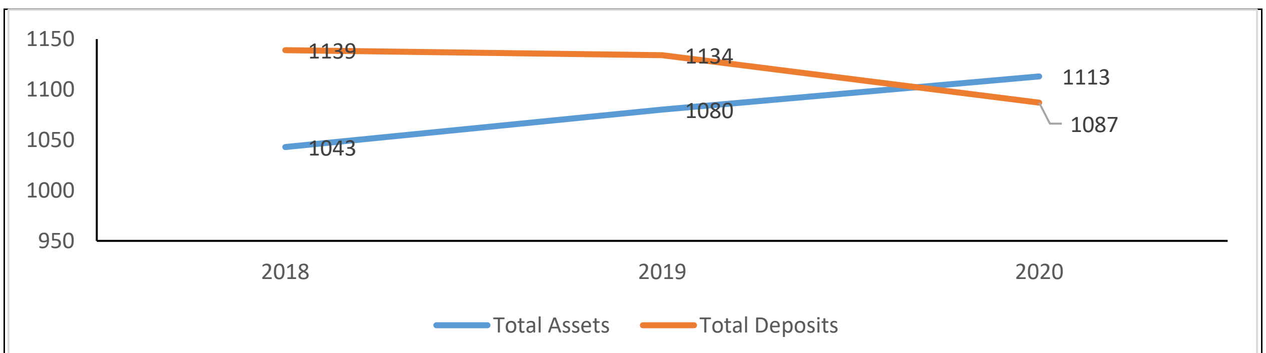
Source FSD, BSL

Box 1. Banking Sector Concentration

The Herfindahl-Hirschman Index (HHI) is used to measure banking sector concentration risk and can be used as an auxiliary tool for supervisory purposes and in the design of macroprudential measures.

The deposit share of the five largest banks in the banking sector declined marginally by 2.25 percentage point from 68.42 in 2019 to 66.17 in 2020. Their asset share also declined by 0.75 percentage points from 65.65 in 2019 to 64.90 in 2020. The HHI index (Figure 12) indicates that the total assets index value increased to 1113 in 2020 from 1080 in 2019 reflecting improvement in the competitiveness of the banking sector. On the same vain, total deposits index value increased to 1187 in 2020 from 1134 in 2019, showing signs of improvement in the banking sector competitiveness. The key point is that a banking sector with an HHI of less than a threshold of 1500 is considered a competitive sector.

Figure 12: Herfindarl-Hirshman Index



Source: FSD, BSL

4.3.1.1 Capital

4.3.1.2 Shareholders' Funds and Regulatory Capital

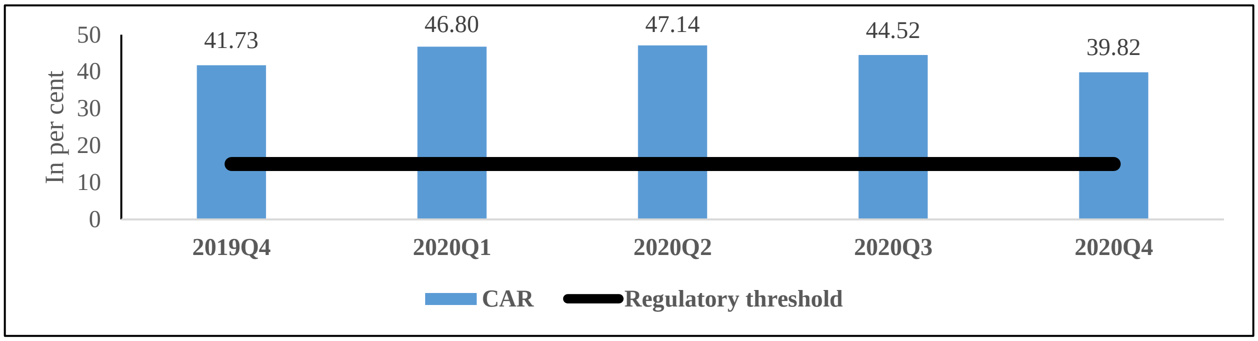
Shareholders' funds grew by 34.87 percent during 2020 while regulatory capital grew by 29.19 percent. This growth in shareholders' funds was as a result of increase in the minimum paid up capital, as banks were required to increase capital to Le65bn by end December, 2020 as well as profits.

4.3.1.3 Capital Adequacy Ratio

The Capital Adequacy Ratio (CAR) of the banking sector fell slightly to 39.82 percent during 2020 attributable mainly to a large increase in risk-weighted assets – the denominator in the ratio – by 35.37 percent. The driver for risk weighted assets is treasury bills and treasury bearer bonds The CAR of the banking sector remained, however, well above the statutory minimum requirement of 15 percent (Figure 13).

All but two banks were able to meet the minimum CAR threshold of 15 percent. Although most banks were able to meet the CAR, only six of the fourteen commercial banks were able to meet the statutory minimum paid up capital requirement of Le65billion for end December 2020 representing 43 percent of the industry. The intuition behind the fact that although vast majority of banks meet CAR less than half of the banks met paid up capital, this is due to the very small risk weighted assets (since government securities have 0% risk weights) hence the capital adequacy ratio will be above the prudential threshold .

Figure 13: Capital Adequacy Ratio (CAR)



Source FSD, BSL

One of the major reasons responsible for the increase in RWA resulted from customers accessing the Special Credit Facility (SCF) that was rolled out by the BSL for the importation of essential commodities to ease the impact of COVID-19 pandemic in 2020. These injections of funds shew up in gross loans and advances over the review period.

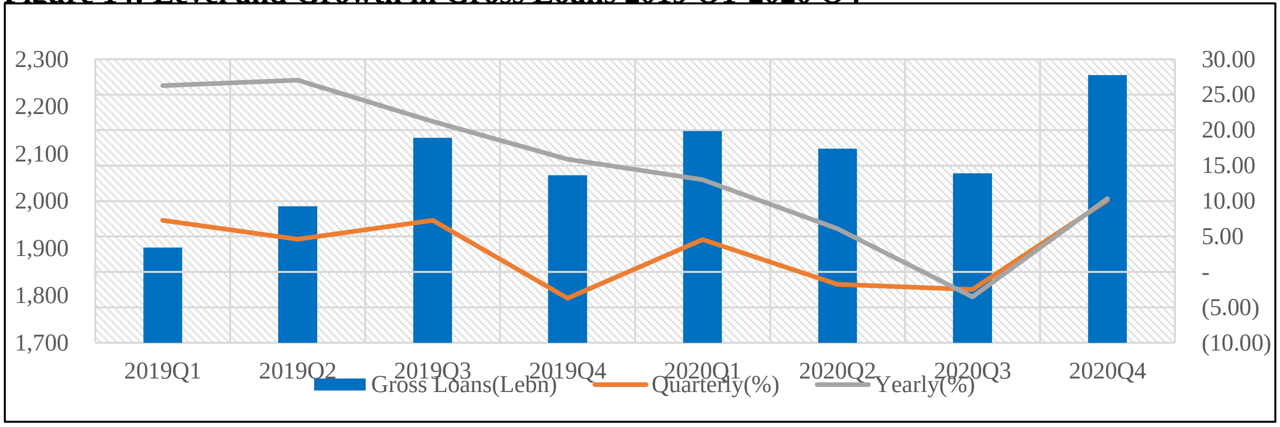
The banking sector recorded a 26.32 percent growth in retained earnings during 2020 with only one of the fourteen commercial banks recording negative retained earnings.

4.3.2 Credit Portfolio

4.3.2.1 Gross Loans

Gross loans and advances increased by 11.35 percent in 2020. This masks, however, an uneven pattern during the year. Loans fell in the immediate wake of the Covid-19 shock (2020 Q2-Q3) but rose significantly in 2020 Q4 due to the Special Credit Facility (SCF) provided by BSL (Figure 14).

Figure 14: Level and Growth in Gross Loans 2019 Q1-2020 Q4



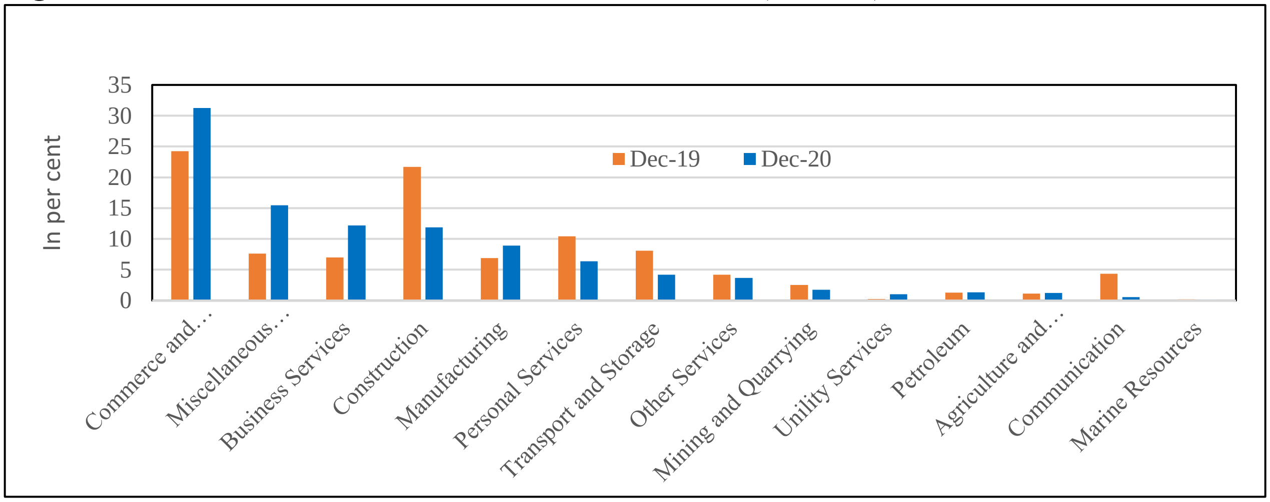
Source: FSD, BSL

4.3.2.2 Sectoral Allocation of Gross Loans

On a sectoral basis, credit has mostly been directed to commerce and finance and the miscellaneous sectors. At end-2020 the commerce and finance sector accounted for almost one-third (31.28 percent) of the industry's total gross loan portfolio.

The increase in sectoral allocation to the commerce and finance sector could also be one of the major reasons for the Leone depreciation as most of the businesses in this sector are engaged in the importation of goods and services, thus putting increasing pressure on the demand for foreign currency. The high exposure to the commerce and finance sector remains among the key risks (concentration risks and credit risks as credit quality worse than other sectors), including foreign exchange risk, facing the banking sector and by extension the financial system. With this structure, shocks to the foreign exchange market will adversely affect the general price levels that could affect the banking sector profitability. This will feed through to loss in the value of the Leone and banks may tend to switch to other forms of investments, mainly T-bills. The current loan to deposit ratio of 36.90 percent is way below the prudential threshold of 80 percent.

Figure 15: Sectoral Allocation of Share of Gross Loans (Percent)



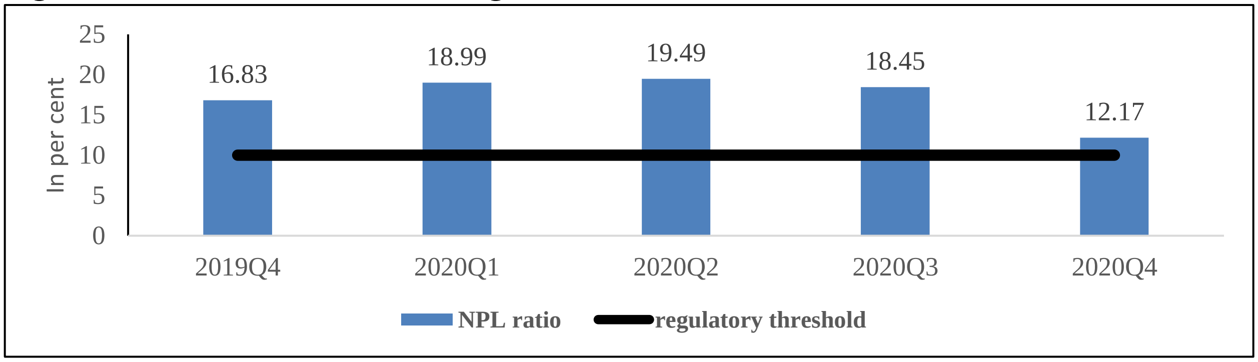
Source: FSD,BSL

The key message from the sectoral allocation of share of gross loans is that in 2020 commerce and finance and miscellaneous categories (individual and personal loans) are leading the way relative to 2019 whilst commerce and finance and construction were leading the way by then. It is pertinent to point out that share of gross loans by sectors is mainly dependent on loan share i.e. sectors which receive the most loans have a bigger gross loans share than sectors that receive few loans.

4.3.2.3 Non-Performing Loans (NPLs)

The NPL ratio fell significantly during 2020 but remained a little above the regulatory requirement of 10 percent (Figure 16).

Figure 16. Trend of Non-Performing Loans Ratio



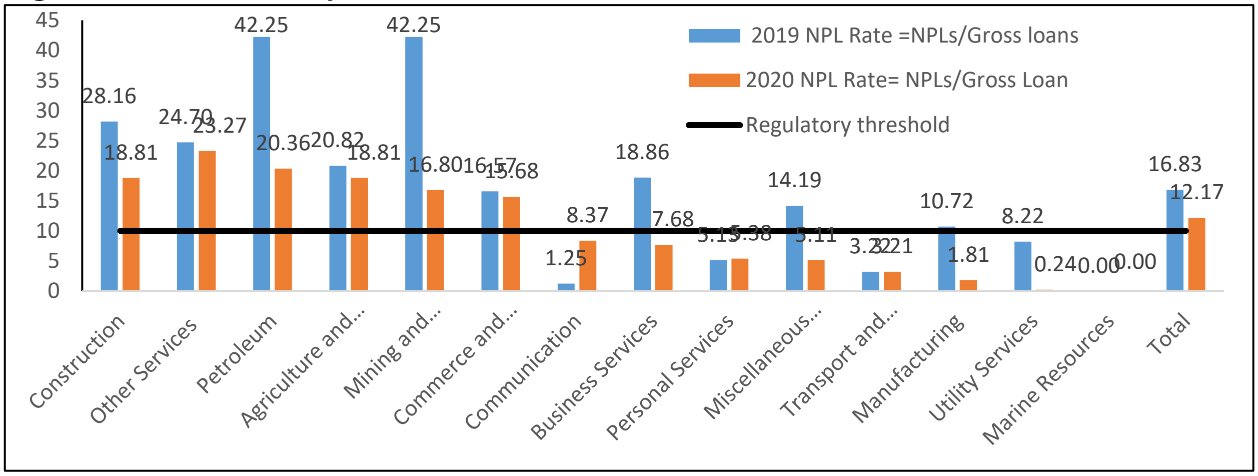
Source: FSD,BSL

The improvement in the NPL ratio during 2020 in the banking sector as a whole was due to (i) government payment of arrears to contractors in the construction sector who, in turn, were able to settle some of their bank debts (already classified as NPLs), (ii) the introduction of the BSL Special Credit Facility (SCF). Bank borrowers were encouraged to pay part or whole of their outstanding bank facilities to be able to access this facility and (iii) full liquidation of loans owed by specific customers in two of the commercial banks.

4.3.2.4 Gross Loans and NPLs by Sectors

Despite a higher share of loans being provided to the commerce & finance sector – a sector with a high NPL rate – this has been more than offset since a lower share of loans in 2020 were made to the construction sector – a sector with a higher still NPL rate – and an increase in the share of loans were made to the business and miscellaneous sectors which have lower than average NPL rates. Also, ten out of the fourteen banks including the two state-owned banks recorded NPL rates below the 10 percent threshold.

Figure 17: NPLs Rate by Sector 2019, 2020 and Total



Source: FSD,BSL

The main point is that the trend of NPL rate by sectors has declined over the review period 2020. The sectors leading in terms of the improvement in asset quality (less than 5 percent) in 2020 are marine resources (0%), utility services (0.24%), manufacturing (1.81%) and transport and storage (3.21%). The sectors were asset quality significantly deteriorated in 2020 include Other Services (23.27%), Petroleum (20.36%) amongst others. On the whole, asset quality improved by 4.66 percentage points in 2020.

Box 2: Credit Reference Bureau (CRB)

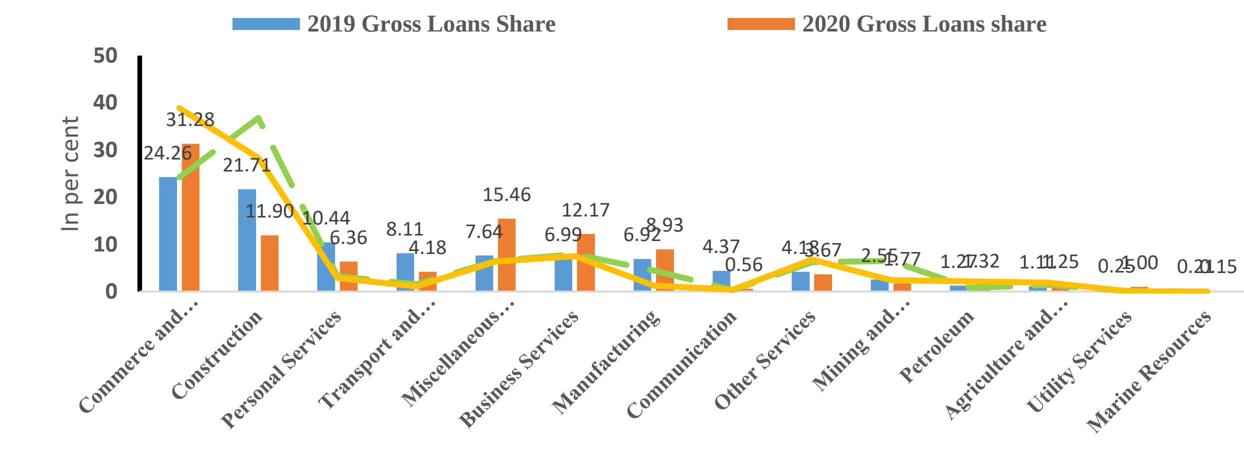
The Bank of Sierra Leone continues to work with KIVA, a Silicon Valley Company to automate the Credit Reference Bureau as well as provide a unique digital ID to solve the challenges of lack of identification. The digital identity verification platform will help financial institutions address the issue of customer identification which is key for the mandatory Know Your Customer (KYC) and Customer Due Diligence (CDD). It would also serve as the unique identifier to provide access to customers' credit reports online. Due to the Corona Virus pandemic, the pilot stage of the implementation was halted as the KIVA technicians moved out of the country. However, the Bank and the management of KIVA are currently in talks on how to proceed given that the agreed timelines have elapsed.

Source: BSD, BSL

4.3.2.5. Credit Growth by Sectors

During 2020, credit to the Business Services, Miscellaneous and Commerce and Finance sectors increased by 93.73 percent, 125.16 percent and 43.46 percent respectively. However, the growth in credit to the construction sector declined by 45.18 percent.

Figure 18: Share of Gross Loans and NPLs by Sector 2019 and 2020



Source: FSD, BSL

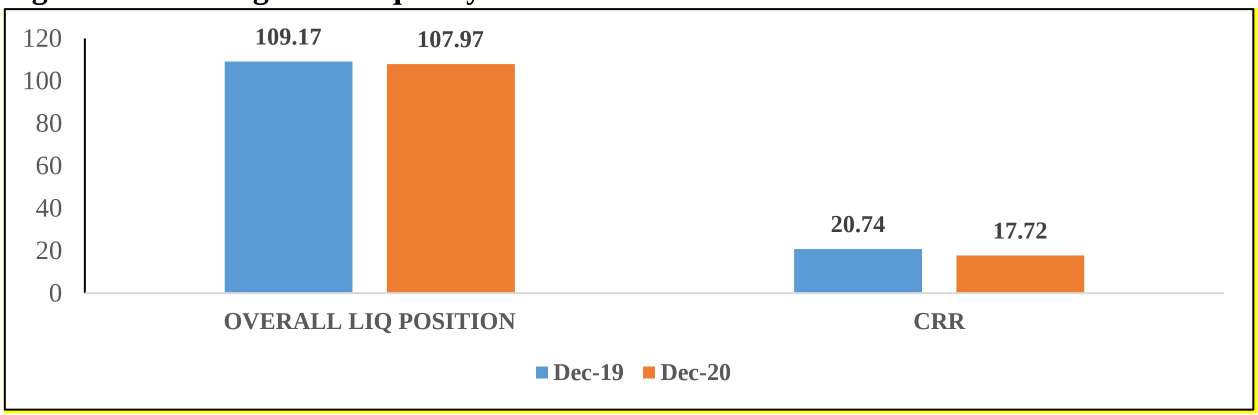
4.3.2.6 Large Credit Exposures

The 50 largest credit exposures accounted for 62.51 percent (Le1,846.30bn) of the banking sector's aggregate exposures in 2020. The largest single borrower exposure to capital base was 15.98 percent in 2020. The level of the 50 largest borrowers of the banking sector is sustainable and the banking sector remains resilient to shocks. Large exposures decreased by 3.80 percent in 2020.

4.3.3. Liquidity Indicators

The cash reserve ratio (CRR) for end December 2020 stood at 20.74 percent, compared to 17.72 percent registered for end December 2019 and was comfortably above the statutory minimum limit of 12 percent. The commercial banks also met the overall liquidity requirements, recording 109.17 percent in 2019 and 107.97 percent in 2020, well above the prudential requirement of 31.03 percent. Furthermore, to support liquidity in the banking sector in the midst of COVID-19 pandemic environment, the Monetary Policy Committee (MPC) extended the reserve requirement maintenance period for commercial banks from 14 days to 28 days.

Figure 19: Banking sector liquidity indicators

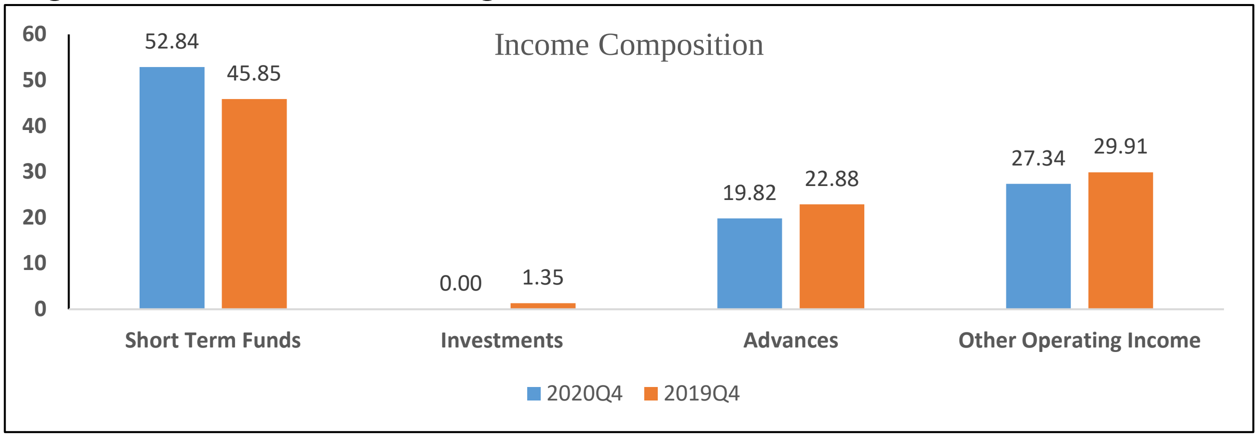


Source FSD, BSL

4.3.4. Earnings

The main earning assets for banks were investments in government securities and loans and advances. As at December 2020, investment in government securities accounted for 52.8 percent while loans and advances accounted for 19.9 percent, both accounting for 72.70 percent of earning assets. Commercial banks continued to increase their holdings of government securities at the expense of lending to the private sector. The asset structure of commercial banks demonstrated that investment in government securities continued to be the banks' main business model, leading to concentration risk, one of the major risks facing the banking sector and the financial system at large. This is the main reason why capital and liquidity ratios are so high. Also at the macro level it stifled lending to the real economy to support potentially higher economic growth .Other operating income accounted for 27.30 percent of income in 2020.

Figure 20: Contribution of earning assets



Source: FSD, BSL

4.3.5. Profitability

Banking sector profits picked-up as income increased in Q4 of 2020 in absolute terms, more than expenditures. Pre-tax profits for the banking sector increased by 21.04 percent in 2020. The growth was largely due to revenues from net interest income which grew by 15.44 percent. Short term investments mainly in government securities accounted for more than half of the banking industry's total income (52.80 percent), interest from loans & advances (19.80 percent), while other operating income contributed 27.30 percent.

On the expenditure side, other operating expenses which included staff and administrative expenses, accounted for 84.85 percent of total expenses, whereas interest expense accounted for 15.15 percent.

4.3.6 Deposits Growth

Total bank deposits grew by 39.20 percent in 2020 driven by deposits from local residents in local currency. The share of foreign currency deposits fell to one-third. Global experience indicates that resident deposits constitute a stable funding source compared to nonresident deposits that are highly sensitive to market sentiments. As at December 2020, interbank and foreign financing represented other sources of financing for banks, at 16.30 and 6.80 percent, respectively. Banks use interbank funds mainly for short-term liquidity management, rather than for investment purposes.

4.3.6.1 Large depositors

The 20 largest depositors accounted for 34 percent of the sector's total deposit whilst the largest depositor accounted for 8.30 percent in 2020. The level of the 20 largest depositors in the sector has a higher sensitivity of sustainability against possible liquidity shocks in the event of any sudden withdrawals by one or more of the largest depositors. Deposit concentration increased from 31.00 percent in 2019 to 34 percent in 2020.

Box 3: Deposit Protection Fund

On the Deposit Protection Scheme, the Bank is well advanced with the development of the Sierra Leone Deposit Protection Scheme (SLDPS) following the Bank of Sierra Leone's Board approval in May 2018. The Bank through the support of a Consultant provided by the US Treasury Department, developed a draft Deposit Protection Bill which will provide the legal framework and the said document has been forwarded to the Ministry of Finance to facilitate Cabinet approval and the final preparation by the Law Officers Departments (LOD), of the Attorney General's Office prior to enactment by the Parliament of the Republic of Sierra Leone. Other administrative and logistical arrangements to support the scheme are well advanced.

Source: BSD, BSL

Box 4: Collateral Registry

On the Sierra Leone Collateral Registry, the Bank of Sierra Leone continues to work with Government of Sierra Leone and the World Bank under the Sierra Leone Economic Diversification Project for the implementation of the phase II of the Collateral Registry Project, which includes the drafting and enactment of a new Borrowers and Lenders Regulation, public education and awareness raising on the collateral registry and the reconfiguration of the Collateral Registry System in line with the new Borrowers and Lenders Act, 2019. The latter would enable individuals and non-incorporated entities (entities other than financial institutions licensed by the BSL) to open an account and register security interests on the Collateral Registry Platform. The Bank has also revised downwards the various fees charged for the use of the Sierra Leone Collateral Registry System in order to enable Micro, Small and Medium Enterprises have access to credit facilities.

Source: BSD, BSL

Box 5: Development in the IFRS 9 Implementation

Based on Development in the IFRS Implementation, the BSL fully implemented IFRS 9 in 2018 for all banks in the industry and had successfully issued an IFRS 9 Implementation Guideline with the support of the Office of Technical Assistance, U.S Treasury. The Post implementation team continues to assess the credit risk model used by banks to monitor the variables incorporated and the respective impact of such variables on the Expected Credit Losses (ECL) of financial institutions.

Source: BSD, BSL

Box 6: Development of IFRS 16

In January 2016, the International Accounting Standards Board issued IFRS 16 on Leases which replaces IAS 17, IFRIC 4, SIC 15 and SIC 27. The BSL noted that banks complied with the financial reporting requirement of IFRS 16 with specific exceptions for a bank with leases of 12 months (as stipulated by IFRS 16:5, 6 & 8). Most banks applied IFRS 16 retrospectively from January 1, 2019 using the simplified retrospective approach.The BSL's financial reporting review team will continue to assess the impact of IFRS 16 on regulatory capital in its Post Implementation Review (PIR).

Source: BSD, BSL

4.3.7 Dynamics of Risk Assessment

The banking sector continue to be over reliant on short term funds that constrain them to finance long-term investments with minimal risk. Deposits represent around 71.95 percent of total liabilities of the banking sector as of December 2020. Around 67.35 percent of total banks' deposits were demand deposits - funds that can be withdrawn without notice. Although maturity transformation is part of the normal business of banks, it can lead to maturity mismatch which is a risk to the banking sector. Additionally, for risk averse banks, short-term resources could limit their ability to underwrite long-term feasible projects with higher returns.

Concentration of loans and advances in the 50 largest borrowers is another key risk which continue to face the banking sector. As at end December 2020, the total outstanding gross loans and advances to the 50 largest borrowers stood at Le1,846.30bn, whilst the banking sector's total regulatory capital stood at Le1,738.94bn. This indicated that the banking loan portfolio was highly concentrated and as a result the returns on the underlying assets could be correlated, implying that a shock to any of these customers in this group would pose significant distress on the banking sector.

Though there is a prudential single obligor limit of 25 percent for secured facilities and 10 percent for unsecured facilities, there is still need for the sector to diversify their clientele by designing products, services and channels which suit their conditions. Competition of a few corporate clients in the 50 largest borrowers group, limits growth of the banking sector and also opens them to potential risks.

Furthermore, diversification of the banking sector loan portfolio and deposits is important for safety and stability of the sector and the system at large.

Box 7: Development in the Risk Based Supervision Implementation

The implementation of the Risk Based Supervision strategy is fully on course following its launch on 1st March 2019. The Banking Supervision Department conducted four (4) examinations in 2020 using the Risk Based Approach despite the threat of the COVID-19 pandemic. The Bank also conducted a webinar for senior staff of commercial banks to discuss the Risk Based Supervision Framework and also discuss the findings from previous examinations and lessons learn.

Source: BSD, BSL

4.4 Financial Markets

4.4.1 Foreign Market Operations

The exchange rate of the Leone broadly reflected developments on the global foreign exchange market as well as domestic demand and supply conditions, including the Bank's interventions in the foreign exchange market. The global foreign exchange market was highly volatile in the wake of the outbreak of the COVID-19 pandemic. This and other domestic challenges adversely impacted the exchange rate. The imposition of national confinement measures in April 2020 resulted in closure of businesses as well as the national borders. Likewise, the tourism and export sectors, in particular, the manufacturing sector, were severely impacted, with limited inflows of foreign exchange earnings and the ensuing influence on the domestic currency.

In spite of these challenges, the Leone/US dollar exchange rate remained relatively stable in 2020, partly due to BSL's action at dampening the effect of exchange rate movement on domestic prices. Furthermore, the increase in foreign currency inflows from Development Partners to support the fight against the COVID-19 Pandemic and the foreign exchange made available under the BSL's Special Credit Facility and foreign currency outright sale transactions with commercial banks in December, 2020 contributed in maintaining the relative stability in Leone/ USD dollar exchange rate. The average mid rates of the official BSL and commercial banks' rates marginally depreciated in the year to end-2020 from Le9,692.90 and Le9,824.68 to Le10,133.90 and Le10,257.50 respectively.

However, the interbank foreign exchange market remains illiquid. The total interbank transactions during the review period amounted to only USD7.50mn.

Notwithstanding the COVID-19 crisis, total diaspora remittances increased by 114 percent in the year to end-2020 to USD135.69mn.

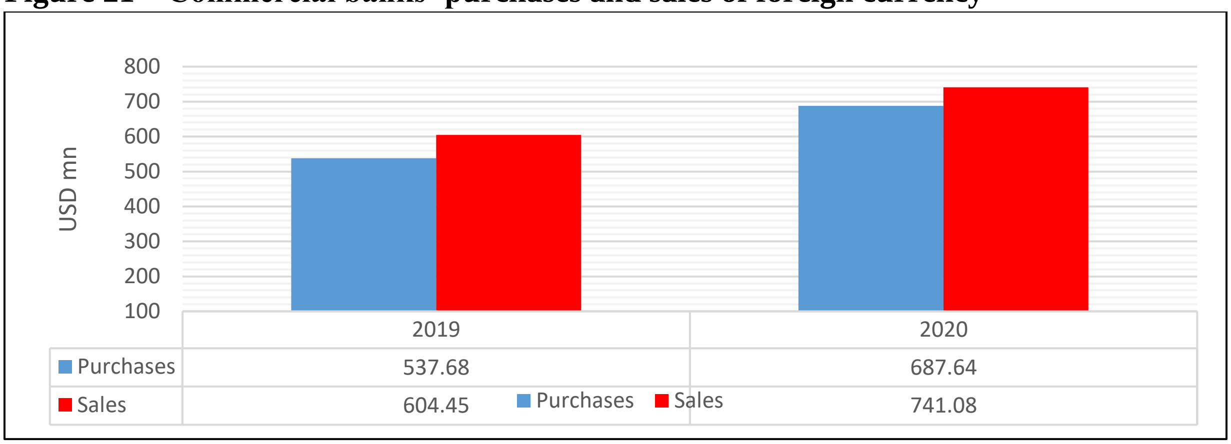
4.4.2 Foreign Exchange Flows

The total amount traded in the foreign exchange market during 2020 was USD3.76bn and was 5.61 percent higher than in 2019. The monthly average amount traded in 2020 was USD0.31bn about the same as in 2019.

4.4.3 Purchases and Sales of Forex by Commercial Banks

Total purchases of foreign exchange in 2020 was USD0.69bn, an increase of 27.78 percent from 2019 levels (Figure 21). The increase was largely due to purchases from the mining sector, International NGOs, Bureaus' remittances, BSL outright sales and the service sector. Total sales of foreign exchange by commercial banks also increased by 23 percent to USD0.74bn in the year to end-2020. These sales were mainly for trade-related payments including fuel and rice imports.

Figure 21 – Commercial banks' purchases and sales of foreign currency

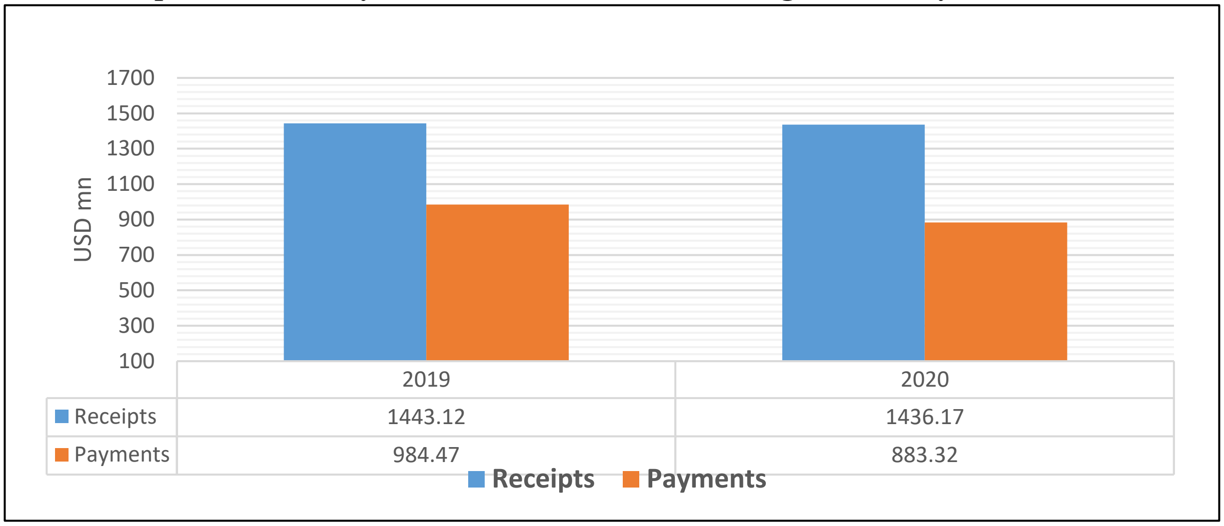


Source: FMD, BSD

4.4.4 Receipts into and Payments from Customers' Foreign Currency Accounts

Receipts into customers' foreign currency (CFC) accounts remained at USD1.44bn in 2020 (Figure 22). This was sustained mainly by Foreign Exchange Bureaus' remittances and BSL outright sales. Payments from customers' foreign currency accounts in 2020 decreased by 10.27 percent in 2020. The payments from CFC accounts/outflows were mainly for trade-related imports and rice whilst payments by oil importing companies, telecommunication companies, diamond exporters, and travel and personal payments decreased slightly.

Figure 22 – Receipts into and Payments from Customers' Foreign Currency Accounts



Source: FMD, BSL

4.4.5 Foreign Exchange Auction

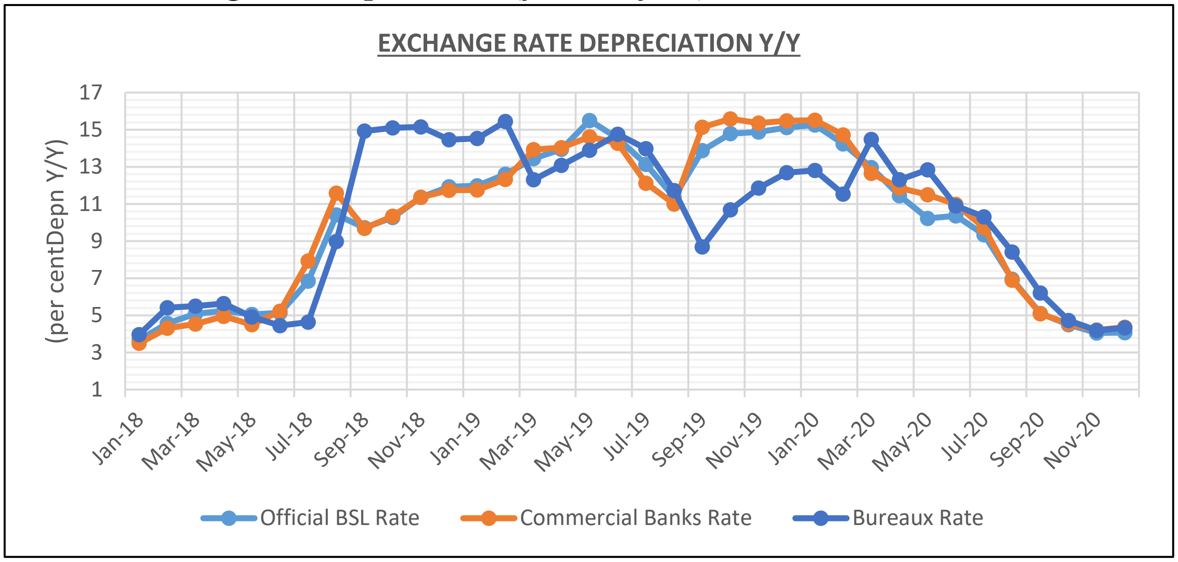
The foreign exchange auctions complements foreign exchange supply in the market and also serves as a signaling mechanism to anchor market expectations and general macroeconomic perception. It also complements monetary operations and provides a means to sterilize the Leones realized from the disbursement of donor funds.

To dampen the foreign exchange demand pressure in August, 2020, the Bank intervened through wholesale foreign exchange auctions to complement the supply of foreign exchange in the market. Three foreign exchange auction sessions were held in August, 2020 with a total amount of USD15.00mn offered, USD13.20mn was demanded and USD12.80mn was supplied.

4.4.6 Foreign Exchange Rate Movements

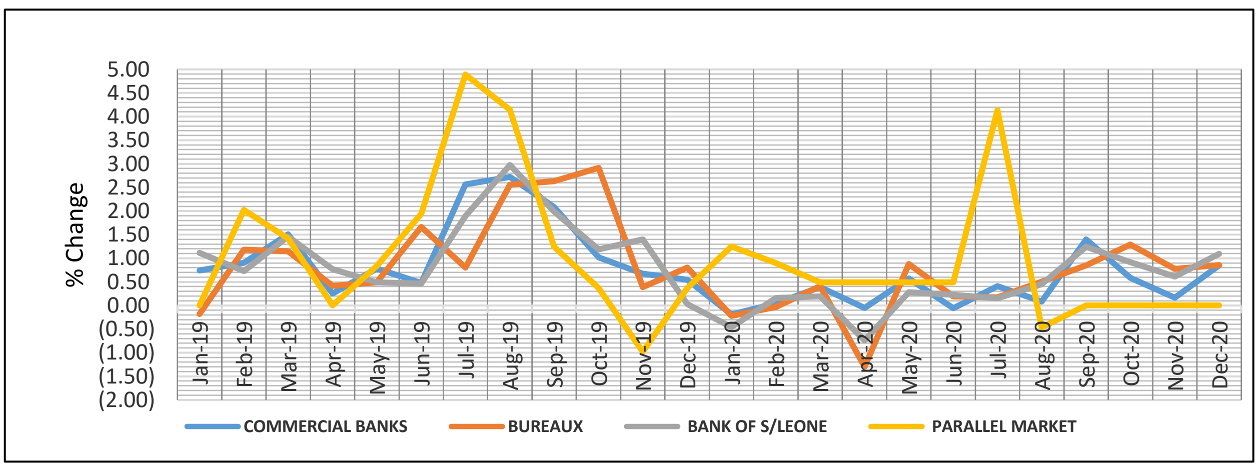
The Leone/US dollar exchange rate remained relatively stable in 2020, partly due to the BSL's administrative measures aimed at dampening the effect of exchange rate movement on domestic prices and cash swap arrangements with commercial banks. In the year to end-2020, the official BSL, commercial banks' and bureaus' exchange rates all marginally depreciated by 4.4-4.6 percent (Figure 23).

Figure 23 – Exchange rate Depreciation (year-on-year)



Source: FMD, BSL

Figure 24 - Exchange Rate Depreciation (month-on month– Jan 2019 to Dec 2020)



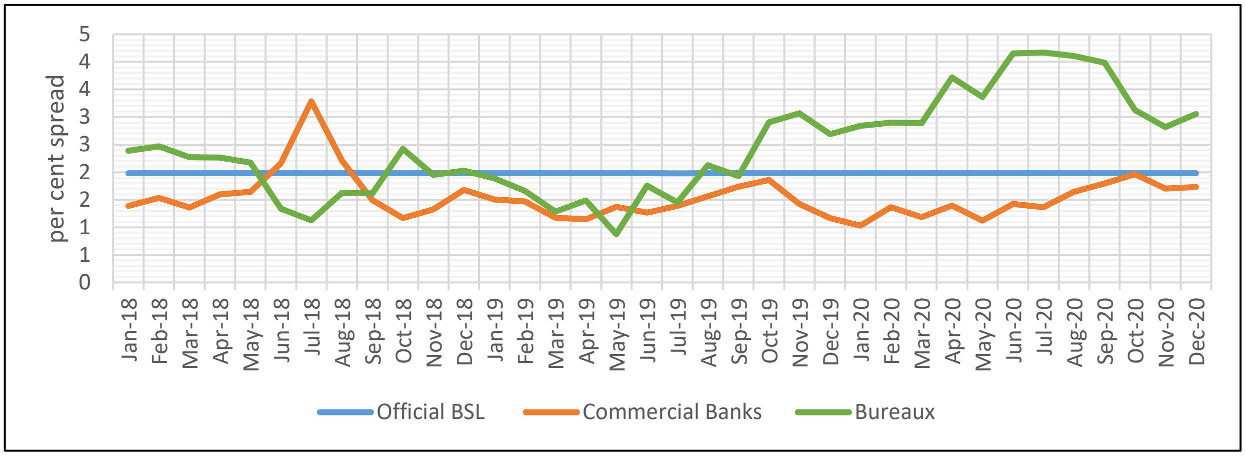
Source: FMD, BSL

The average Leone/ US Dollar exchange rate also remained relatively stable on a month-on-month basis with intermittent convergence between the official BSL rate and commercial banks rate.

4.4.7 Spread in the Various Markets

The spread between the average official BSL foreign currency buying and selling rates remained constant at 1.98 percent. The foreign currency spreads at commercial banks and bureaus increased during 2020 Q2-Q3 in the wake of the COVID-19 crisis but narrowed in 2020 Q4 (Figure 25). The latter reflected an easing of conditions in the foreign exchange market with its attendant stability in the market exchange rate.

Figure 25 – Average Monthly Percentage Spread in the Different Exchange Rates Markets



Source: FMD, BSL

4.4.8 Market Outlook

The stability of the exchange rate is expected to be sustained in the near to medium term, in line with expected increase of public and private investments in agriculture, fisheries and tourism as part of Government's effort to diversify the economy. Furthermore, the resumption of iron ore exports and the expansion of diamond and rutile production may increase export receipts and gross foreign exchange reserves. The downside risk, however, is the spread and containment measures of the third wave of COVID-19 pandemic that may put upward pressure on inflation and downward pressure on foreign exchange reserves and the Leone.

4.5 DOMESTIC MARKET AND MONETARY POLICY OPERATIONS

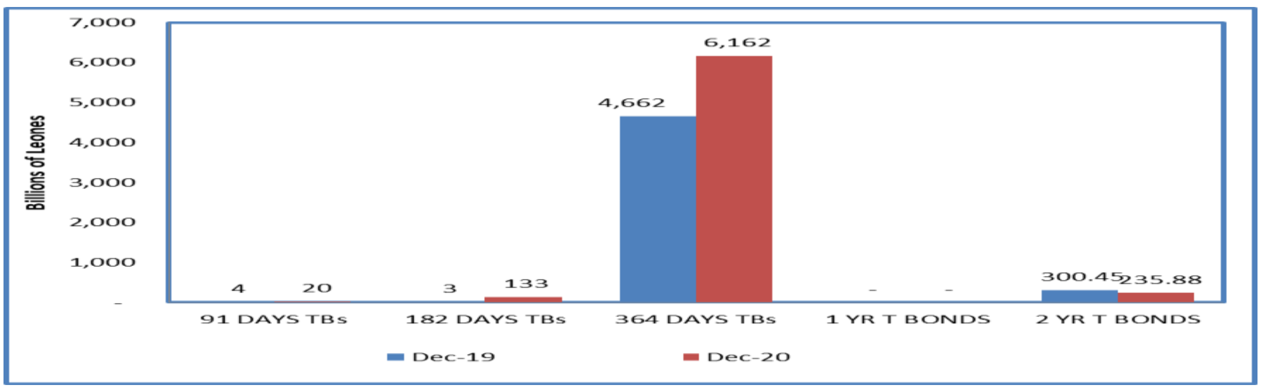
4.5.1 Primary Market Auction Outcomes

During 2020 the primary market auctions for Government Securities exhibited mixed outcomes. The 91-days and 182-days tenures were oversubscribed in the first three quarters of 2020 but under-subscribed in the fourth quarter, whilst the 364-days tenure was mostly oversubscribed throughout the year. As such, the demand for government treasury bills was skewed towards the 364 days tenure, with commercial banks, being the leading participants. However, the non-bank public continued to be the dominant participant in the 91-days and 182-days tenures of the treasury bills auctions.

4.5.2 Stock of Government Securities

The total stock of Government securities increased by 27.86percent in the year to end-2020. Marketable securities – which accounted for 90 percent of the total stock – increased by 31.86percent, largely on account of an increase in 364-days T-bills (Figure 26). The issuance of new treasury securities during the year was mainly to finance the government's budget deficit.

Figure 26: Stock of Marketable Government Securities by Tenure



Source: FMD, BSL

4.5.3 BSL Standing Facilities

Access to the BSL Standing Lending Facility (SLF) window decreased by 90.21percent during the year to end-2020. This was mainly owing to the excess liquidity position of banks, especially in 2020 Q3-Q4, resulting from donor disbursements for budget financing and balance of payments support to reduce the economic impact of the COVID-19 Pandemic. In the Standing Deposit Facility (SDF) window, the volume of transactions in the year to end-2020 increased almost ten-fold from Le546bn to Le5,552bn, reflecting the improvement in liquidity conditions in the banking system.

4.5.4 Secondary Market Operations

In 2020 the volume of interbank transactions decreased by 35.4 percent whilst The Bank's outright purchases of Treasury Bills in the secondary market fell by 21.5percent.

CHAPTER FIVE

5.0 NON-BANK FINANCIAL SECTOR

5.1 Overview

The non-bank financial sector has been growing in recent years with Microfinance Institutions accounting for almost one half of the sector's total assets. Total asset grew by 6.70 percent in 2020 and is expected to continue to grow over the medium-term as more institutions enter the market, especially in microfinance.

Table 7: Assets of non-bank financial institutions by type (billions Leones)

Types	**2019**	**2020**	**percent Change**
Insurance Companies	330.68	347.22	5.00
Pension Fund/ NASSIT	2,189.09	2,350.98	7.40
Microfinance Institutions	2,433.93	2,567.86	5.50
Community Banks	90.24	110.34	22.27
Financial Services Associations	59.4	69.00	16.16
Total/ Change	**5,103.34**	**5,445.40**	**6.70**

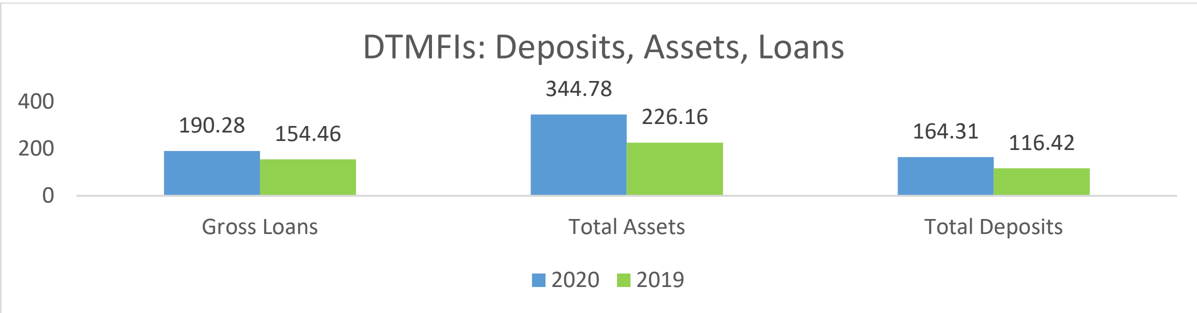
Source: OFISD, BSL

5.2 Other Financial Institutions

5.2.1 Deposit Taking Microfinance Institutions (DTMFIs)

The financial performance of DTMFIs improved in 2020. Their assets increased by 52.5 percent from Le226.16bn in 2019 to Le344.78bn in 2020. Total deposits and gross loans also increased substantially (Figure 27).

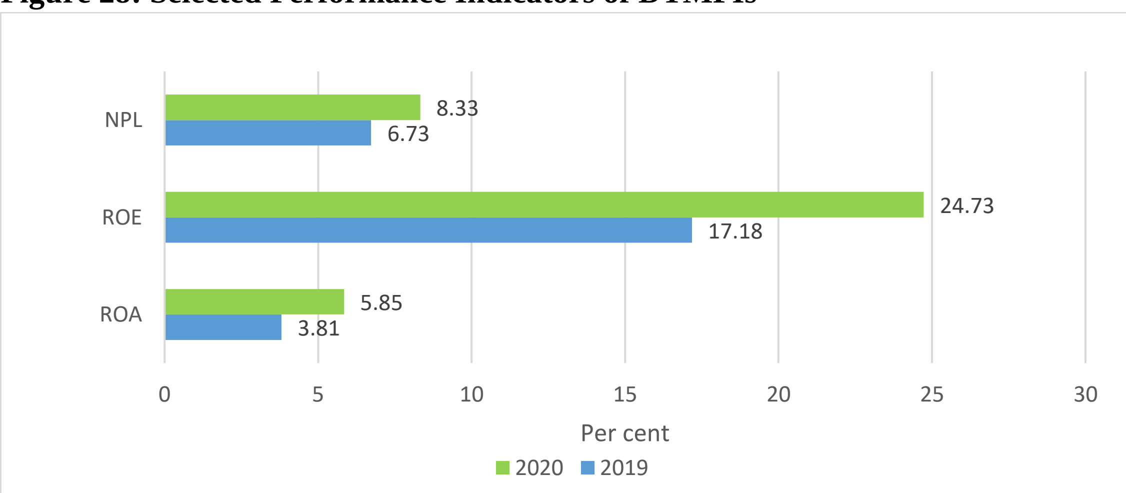
Figure 27: Deposits, Loans, and Assets of DTMFIs, 2019-2020



Source: OFISD, BSL

The profitability of DTMFIs measured by both ROA and ROE also improved significantly despite the COVID-19 pandemic (Figure 28). This indicates that DTMFIs are more efficient in their use of assets to generate income and earnings for their shareholders. However, the asset quality of the DTMFIs declined as reflected in an increase in NPLs. This reflected the impact of the COVID-19 pandemic on some sections of the trade and commerce sector that utilize the services of DTMFIs.

Figure 28: Selected Performance Indicators of DTMFIs



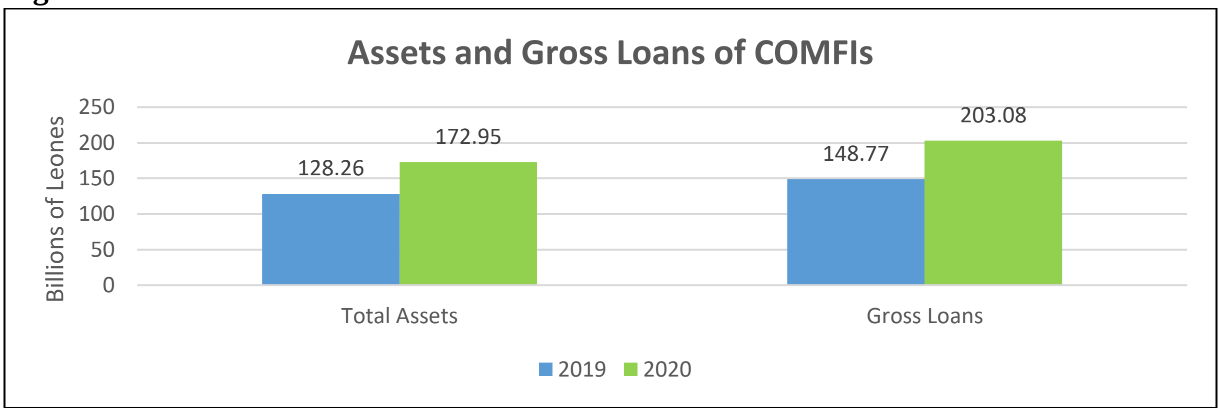
Source: OFISD, BSL

Portfolio at Risk (PaR) ≥ 15 days. Overall, at end- 2020, the portfolio risk ratio for DTMFIs as a whole was 8.33 percent, well above the required MIX minimum standard of 4.8 percent. That said, three DTMFIs failed to meet this MIX standard implying the need for substantial improvements in credit management and loan recovery strategies.

5.2.2 Credit-only Microfinance Institutions (COMFIs)

In the year to end-2020, the assets of COMFIs increased by 36.5 percent reflecting mainly an increase in gross loans (Figure 29). Total equity of COMFIs increased by 43.4 percent reflecting a huge increase in reported paid up capital and prior year retained earnings.

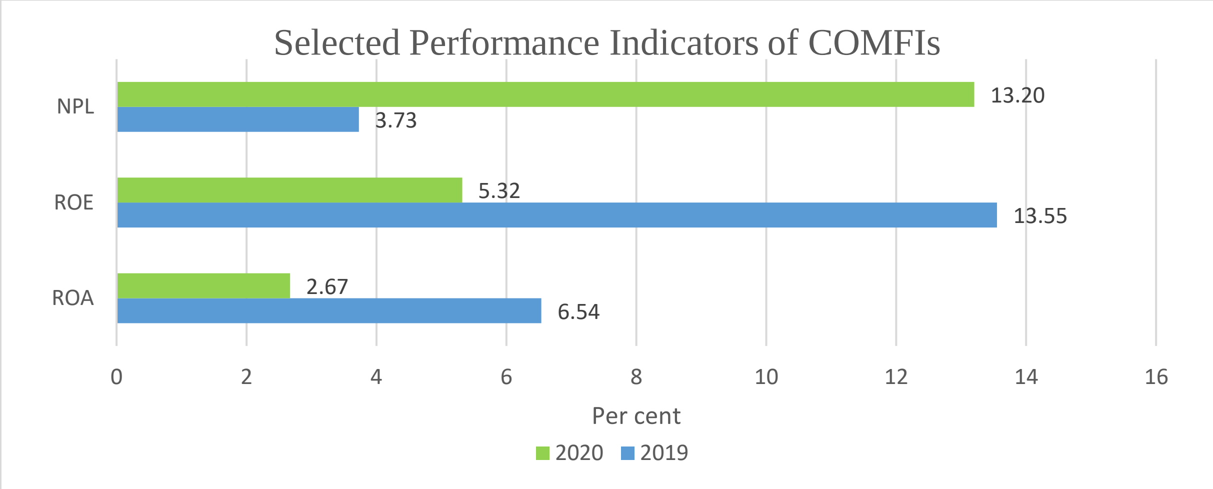
Figure 29: Assets of COMFIs



Source: OFISD, BSL

However, COMFIs' profitability and asset quality fell sharply in 2020. The ROA and ROE fell to 2.67 and 5.32 percent in 2020 respectively and NPLs increased to 13.20 percent (Figure 30). This poor financial performance likely reflects the impact of the COVID-19 pandemic on SMEs, especially those in the trade and commerce sector, who are the main customers of COMFIs.

Figure 30: Selected performance indicators of COMFIs



Source: OFISD, BSL

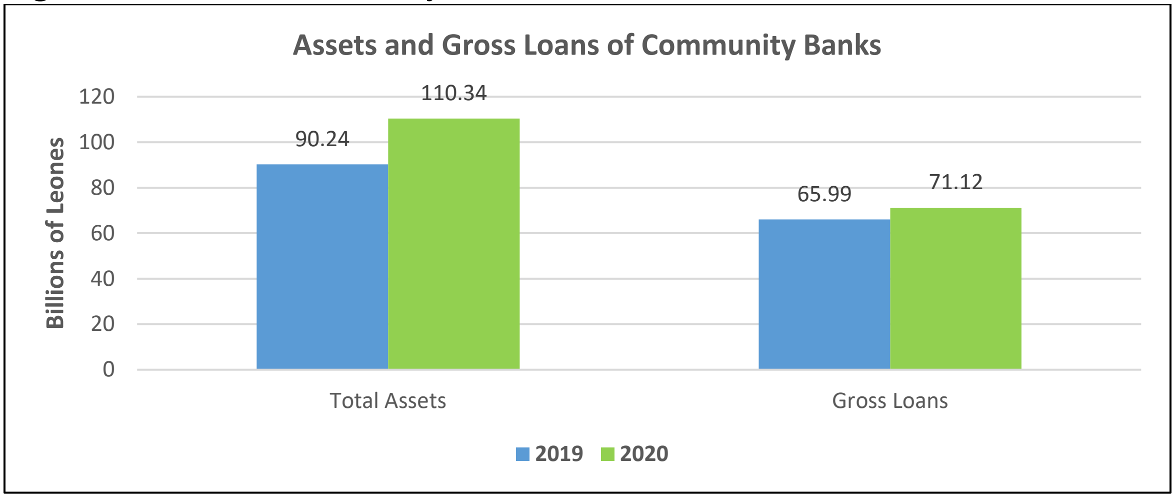
Portfolio at Risk > 30 Days

Consolidated Portfolio at Risk (PaR) for all eighteen COMFIs covered in this report stood at 13.20 percent in December 2020. The highest PaR recorded was 91.75percent and the least was 3.51percent. Individually, six out of eighteen COMFIs covered in this report met the MIX requirement and out of the six, four recorded nil PaR indicating that all their loans are in current category and are performing.

5.2.2.1 Community Banks (CB)

The assets and loans of the community banks increased by 22.3 percent and 7.8 percent respectively in the year to end-2020 (Figure 31). Three CBs account for 40 percent of the total assets of community banks. The increase in the asset base was attributed mainly to an increase in deposit mobilization (34.6 percent).

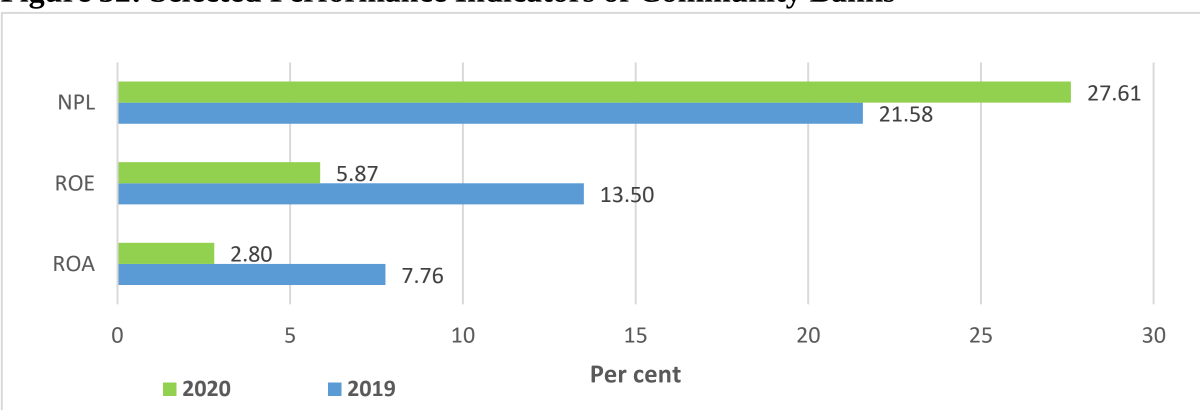
Figure 31. Assets of Community Banks



Source: OFISD, BSL

The profitability and asset quality of the CBs also deteriorated significantly in 2020. The ROA and ROE decreased to 2.8 percent and 5.9 percent respectively whilst NPLs increased to 27.6 percent (Figure 32). This poses a serious challenge to the soundness and resilient of the community banks.

Figure 32: Selected Performance Indicators of Community Banks



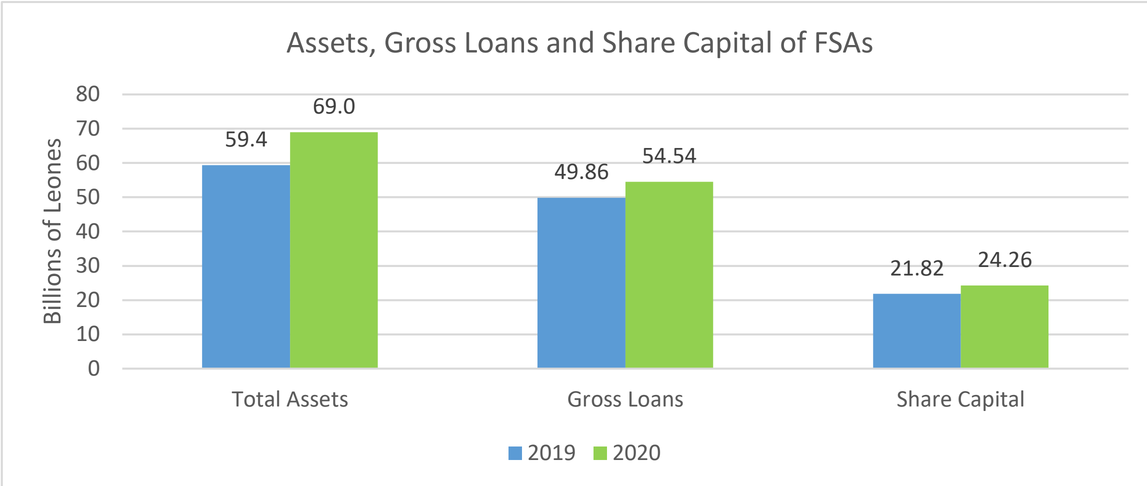
Source: OFISD, BSL

All CBs recorded PaR>30 days far above the tolerable limit of 4.8 percent, implying that the loan portfolios of these CBs are at a higher risk and there is a high potential for future losses.

5.2.2.2 Financial Services Associations (FSAs)

The asset and loans of the FSAs increased by 16.2 percent and 9.3 percent respectively (Figure 33) in the year to end-2020. The increase was driven by an increase in share capital (11.1 percent).

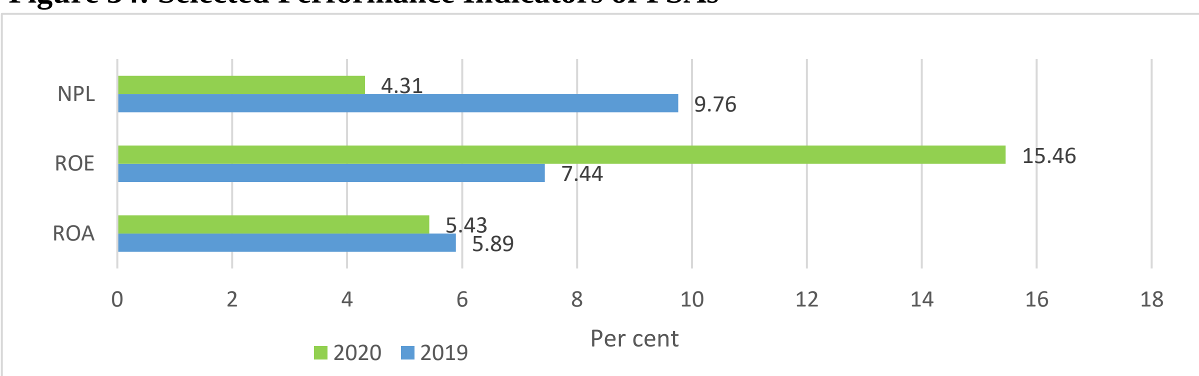
Figure 33: Activity of the Financial Services Associations (FSAs)



Source: OFISD, BSL

The FSAs continue to maintain profitability whilst asset quality improved in 2020. Although the ROA ratio fell slightly the ROE increased significantly and met the minimum MIX requirement of 13.7 percent (Figure 34). The FSAs met the MIX standard of 4.8 percent NPL as it declined to 4.31 percent in December, 2020 from 9.76 percent in December 2019.

Figure 34: Selected Performance Indicators of FSAs



Source: OFISD, BSL

5.2.2.3 Mobile Money Providers

There are three licensed mobile money financial service providers in Sierra Leone – Orange Mobile Finance, AfriMoney and QMoney. Significant increases were recorded in the activities of the mobile money providers as the number of agents, active accounts, transactions, and value of transactions all increased over the year. However, there was a decrease in the number of accounts (Table 8).

Table 8: Activity of the mobile money providers

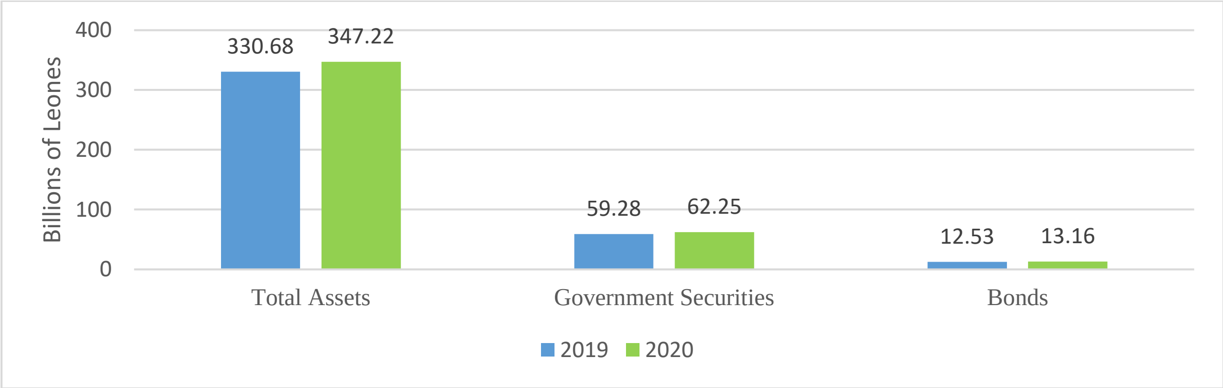
Activity	2019	2020
Number of Agents	18,266	24,120
Number of Accounts	5,944,912	4,279,918
Number of Active Accounts	1,256,118	2,029,439
Number of transactions	42,704,985	59,150,786
Value of transactions (Le'trn)	5,497.33	8,342.86

Source: OFISD, BSL

5.3 The Insurance Sector

The assets of the insurance industry increased modestly in 2020 (5 percent). The low growth in insurance sector may be attributed to COVID-19 pandemic, that dampened economic activities relative to the banking sector wherein BSL introduced Special Credit Facility to assuage the impact of COVID-19 pandemic.

Figure 35: Assets of the insurance industry



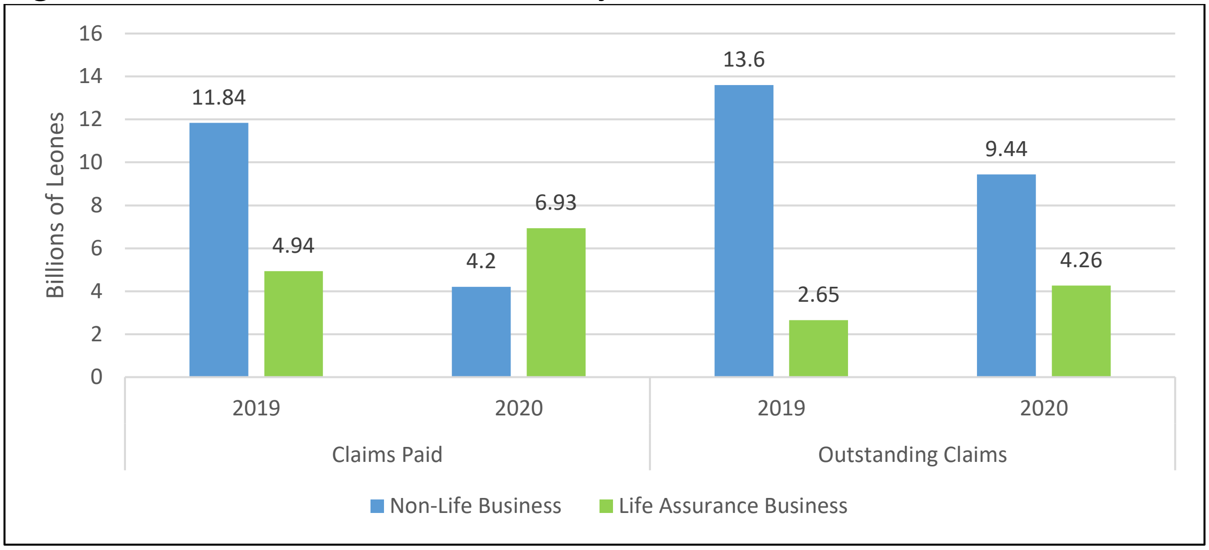
Source: SLICOM

5.3.1 Risk Assessment of the Insurance Industry

The insurance industry in Sierra Leone remained relatively stable in 2020. Genuine claims were honored by all insurers and all registered insurance companies are protected by adequate reinsurance arrangements.

However, life insurers have experienced unprecedented claims by customers. Claims on life insurers increased by 40.38 percent from Le4.94bn in 2019 to Le6.93bn in 2020 as shown in Figure 36. This surge was triggered by the mass retirement of government workers who were insured by these insurers. The Commission has put mechanism in place to manage the risk that might be posed by aggrieved claimants.

Figure 36: Claims on the Insurance Industry



Source: SLICOM

5.3.2 Policy Prescription and Outlook

In order to continue to maintain the stability of the insurance sector, the Commission has engaged the insurers and brokers with a view to increase the minimum statutory and paid-up capital. The recapitalization should further strengthen the stability of the insurance sector, and enhance growth and development.

In a bid to decentralize the Commission, the Commission has established branch offices in Bo, Kenema and Makeni. Personnel in the branch offices will help in propagating the compulsory insurance products thereby leading to increase penetration and growth.

5.4 National Social Security and Insurance Trust (NASSIT)

5.4.1 Key Challenges

The COVID –19 pandemic has negatively affected the NASSIT. The inadequate health infrastructure, poor investment environment worsened the situation and the effect on the operations of the scheme has been unsatisfactory. To address this situation, the Trust adopted an aggressive strategy to improve compliance and reduce administrative costs.

Although compliance remains a perennial challenge for both the private and public sectors, the newly established social security court should prove to be a long-term solution.

5.4.2 Policy Prescription/Ongoing Efforts

The NASSIT Management has directed attention to specific areas that are critical to the long-term sustainability of the scheme in the face of a volatile economy. These areas include the following:

- Continue rebranding NASSIT and improving its public image, especially in the area of service delivery
- Ensure sufficient liquidity for benefits payment and operating expenses, through the development of a feasible funding policy.
- Improve investment performance and enhancing compliance
- Review the current NASSIT Act No. 5 of 2001.

CHAPTER SIX

NATIONAL PAYMENTS SYSTEM

6.0 Introduction

Given the importance of financial market infrastructure, The Bank of Sierra Leone continues to monitor and assess its safety and efficiency.

6.1 National Payments System Landscape

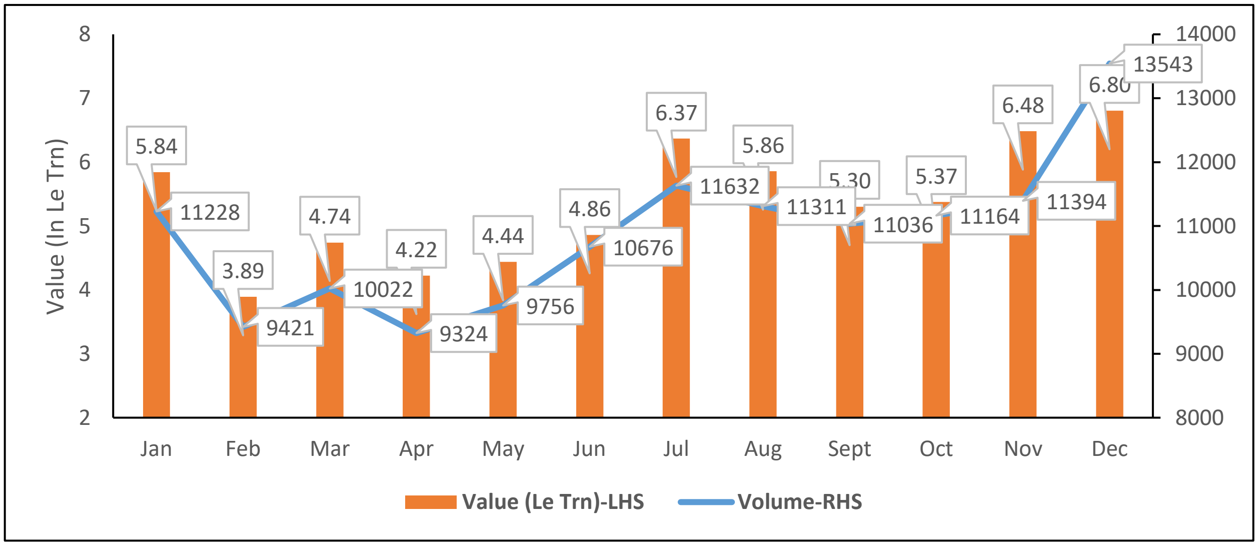
The payments system in Sierra Leone continues to be dual with the coexistence of cash and non-cash based transactions. The volume of cash transaction is still high although non-cash transactions have increased. Non-cash is categorized into retail and large value transactions based on the value of the transactions.

6.1.1 Developments in the National Payment System Landscape

6.1.2 Real Time Gross Settlement (RTGS) system

The Real Time Gross Settlement (RTGS) is an electronic funds transfer system for the settlement of payments across the country. Through the RTGS, transactions are settled and funds can be transferred between participating financial institutions on a real time basis. The volume and value of monthly RTGS transactions in 2020 were at a trough in February but rose gradually and peaked in December during the festive period (Figure 37).

Figure 37: The Volume and Value of RTGS Transactions in 2020



Source: Banking Department, BSL

6.1.3 Automated Clearing House (ACH) Transactions in 2020

The ACH is the retail payment system through which a vast number of payments (both paper-based and electronic) are cleared. These are mainly low-value (up to fifty million Leones), high-volume retail payment cheques.

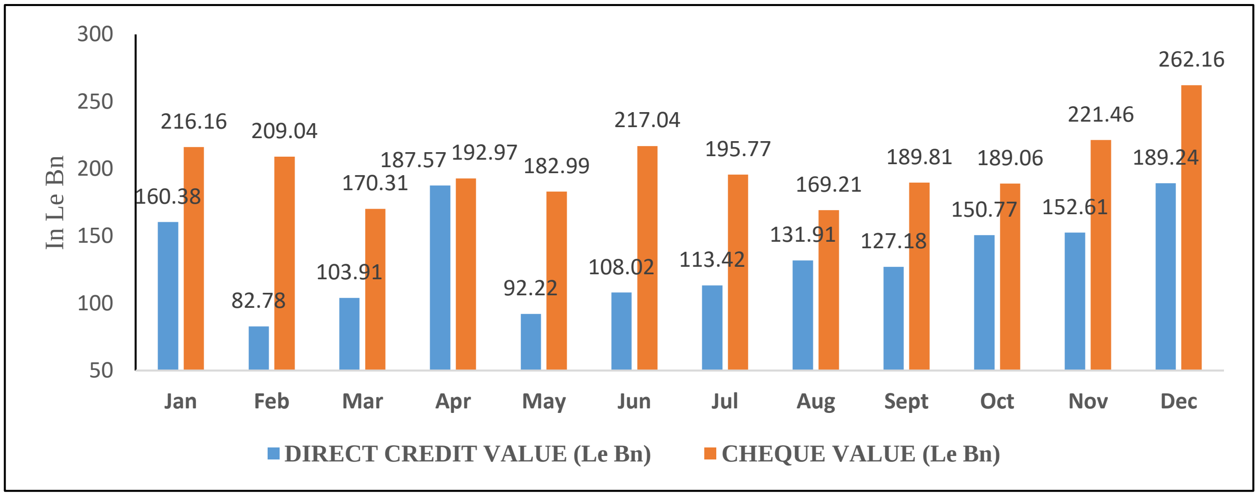
Table 9: Automated Clearing House (ACH) Payments in 2020

Month	Direct Credit Vol	Direct Credit Value (Le Bn)	Cheque Volume	Cheque Value (Le Bn)
Jan	22,210	160.38	15,761	216.16
Feb	15,960	82.78	14,803	209.04
Mar	21,676	103.91	17,569	170.31
Apr	18,809	187.57	12,654	192.97
May	18,097	92.22	11,725	182.99
Jun	22,006	108.02	23,619	217.04
Jul	22,774	113.42	13,277	195.77
Aug	22,851	131.91	12,395	169.21
Sept	23,383	127.18	13,706	189.81
Oct	26,487	150.77	13,974	189.06
Nov	30,114	152.61	14,900	221.46
Dec	33,763	189.24	17,468	262.16
Total	**278,130**	**1,600.02**	**181,581**	**2,416.01**

Source: Banking Department, BSL

In 2020 the use of cheques still remained higher in value terms than direct credit as a means of payment (Table 9). However, the use of direct credit as a means of interbank payment is the prospect to improve in the near future.

Figure 38: Value of ACH Transactions



Source: Banking Department, BSL

6.2 Other Retail Payment Systems

The performance in the value of direct credit transactions as in table 9 above is reflected in the growth of other forms of electronic retail payment systems such as ATM and POS transactions. In table 10 it is revealed that the number of ATMs increased by 20.6 in 2020 while the number of point of sales (POS) declined by 7.50 percent. This further points to the gradual acceptability of electronic means of processing payments.

Table 10: ATM and POS Transactions

	2018	2019	2020
Number of ATMs	72	107	129
Number of POSs	231	301	280
Volume of ATM Transactions	1,204,162	2,199,500	5,740,471,240
Volume of POS Transactions	30,537	40,815	60,383
Value of ATM Transactions (Le Bn)	267.24	392.02	475.24
Value of POS Transactions (Le Bn)	44.1	71.97	58.38

Source: Banking Department, BSL

In line with the Bank's strategy for financial inclusion, ATMs and POSs need to be distributed across the whole country. However, currently most of these facilities are deployed in the Western Area. Even though the Bank has made gains in the public acceptability of electronic payment system, there remains an uneven distribution of these payment services thereby financially excluding a large share of the population.

The above scenario is worthy of note in the midst of plans to implement a digital financial services infrastructure that would ensure smooth flow of funds especially from Government to people (G2P).

6.3 Planned Systems

6.3.1 National Switch

This is a World Bank funded project which targets establishing the interconnectivity and interoperability of all retail payment infrastructure in the financial system by providing a national switch and also help improve rural connectivity. The contract to procure the switch has been awarded to the winning bidder. Also, the services of a National Switch and a Payment System Consultant have been procured. The project has been scheduled to 'Go live' at the end of 2021.

6.3.2 Electronic Fund Transfer (EFT) Project

This is a project funded by the Ministry of Finance to facilitate the interoperability between the Bank of Sierra Leone's Core Banking Application T24 and the Accountant General's Integrated Financial Management Information System (IFMIS), to eradicate the manual processing of payment instruments to banks through cheques and letters. The implementation of this project is at the Test-Run stage.

6.3.3 Review of the Payment System Act (2009)

Given the marked changes in the payment and settlement landscape, BSL has revised the 2009 Payment Systems Act and it is awaiting to be passed into law by the Parliament of Sierra Leone.

6.3.4 AFREXIMBANK – Pan African Payments and Settlement Platform (PAPSP)

Afreximbank, in collaboration with WAMI, is working on a payments and settlement platform to resolve the challenge of interconnecting and interoperating the national payment systems within WAMZ and subsequently ECOWAS so as to promote regional trade.

The platform is now at the stage where settlement accounts have been opened and is awaiting signature specimen for the account.

6.4 Conclusion

Given the increase in the acceptability of electronic payment systems in the country, there is a need to improve the existing market infrastructures and to establish or deepen the payments systems landscape. It is against this backdrop that the Bank of Sierra Leone is supporting the establishment of the National Switch, the EFT with the Accountant General, the PAPSP and also the review of the Payment Systems Act (2009).

CHAPTER SEVEN

7.0 OUTLOOK

Global output is forecast by IMF to grow by 6 percent in 2021 from -3.2 percent in 2020 and 4.9 percent in 2022. The projections assume containment and eradication of COVID-19 pandemic going forward.

The Sierra Leone economy is projected by IMF to grow by 3.00 percent in 2021, reflecting the assuaging impact of the COVID-19 pandemic, given the administration of vaccines and full resumption of economic activities in key sectors of the economy. Furthermore, Sierra Leone's economy is expected to rebound to 3.6 percent in 2022, driven by the fiscal, monetary and structural measures put in place, a likely extension of BSL's Special Credit Facility to enable the private sector to thrive, and facilitate resumption of iron-ore mining and exports.

The financial system's outlook is positive, as evidenced by the trend in most of the key financial soundness indicators buttressed by enhanced supervisory and regulatory framework of the banking system in 2020 regimes. BSL issued additional measures to combat unlawful trading in foreign currency to strengthening financial sector stability. Moreover, the BSL issued guidelines on the Regulatory Sandbox Program; Applications and list of Essential Commodities for BSL COVID-19 Special Credit Facilities; Directives on Suspension of Payments of Dividends for Financial Years 2019 and 2020;Directives on Tiered KYC, Rules for Administering BSL's Special Credit Facility; National Financial Literacy Framework (2020-2024) and Guidelines on Use of Agents.

The outlook for OFIs is tepid as suggested by the improvement in financial health indicators and this will transmit to support financial system stability. More specifically, insurance and pensions institutions are expected to thrive and be resilient to any shocks going forward.

On financial inclusion, the expectation is that it will continue to improve given BSL's continued innovative activities such as Fin-Tech products, services, and solutions.

The World Bank's FSAP is expected to further strengthen the crafting of financial system stability measures from both a micro-prudential supervision and macro-prudential surveillance of the BSL. (This will enable BSL to address some of the challenges in the banking sector, thereby contributing to safeguards of financial system stability).

The BSL's payments system transformation initiatives are expected to boost efficiency and security of transactions in the financial system. The National Payment Switch installation is expected to be completed in 2022 and the gains anticipated include establishment of interconnectivity and interoperability of all retail payment infrastructure for efficiency in the financial system.

7.1 IMPLICATIONS OF THE COVID-19 PANDEMIC ON THE ECONOMY AND FINANCIAL SYSTEM OF SIERRA LEONE

The Bank of Sierra Leone put in place measures to safeguard financial system stability against the COVID-19 pandemic. These measures include creation of Le500.00bn Special Credit Facility to finance the production procurement and distribution of essential goods and services; providing forex resources to the private sector for the importation of essential commodities; and liquidity support to the banking sector via extension of the reserve maintenance period; and reducing the monetary policy rate to encourage lending by banks. The Special Credit Facility is expected to be continued if the COVID-19 pandemic persist for the greater part of 2021.

The Government too was proactive in putting in place measures to help ensure a stable supply of essential commodities, including to address food security concerns; ramped up social protection; and provided support to the private sector, in particular to support small and medium-sized enterprises.

Looking ahead, while the Sierra Leonean economy has great potential, the immediate outlook is likely to remain overshadowed by the ongoing COVID-19 pandemic. Based on programmed policies, growth was projected by IMF to average around 4.5 percent over the medium term. However, prospects for 2021 are subject to considerable uncertainty and will depend significantly on the extent of prevention and containment measures—nationally, regionally and globally—and the associated economic spillovers. The COVID-19 pandemic shock will add to the country's vast development challenges, requiring further support from development partners.

That said, the Agricultural sector is forecast to largely recover in 2021 on account of an increase in food and non-food crop production and in fishing activities. The sector will benefit from reforms being implemented to increase private sector participation in procurement and distribution of inputs to farmers. The services sector is also projected to largely rebound following resumption of international flights, recovery in trade and tourism and transport. The Sierra Leone economic diversification project is expected to revive the manufacturing sector, thereby rebranding the country as an attractive investment destination. In the projected post-COVID-19 pandemic, the government plans to intensify its fiscal consolidation efforts which are expected to reduce the fiscal deficit to 3.6 percent in 2022. This forecast is underpinned by the impact of continued implementation of revenue enhancing measures including the operationalisation and broadening of the Treasury Single Account, deployment of the Integrated Tax Administration System to automate customs and tax collection processes, implementation of the duty and tax waiver policy; and the continued implementation of the liberalized petroleum pricing formula.

With regards to revenue mobilization, total revenue and grants is projected by IMF at Le9.26trn (19.4 percent of non-iron-ore GDP) in 2021. This is driven by the significant resumption of economic activities that boost domestic private consumption, the businesses climate, and pickup in employment levels that, in turn, boost corporate and personal income taxes, mineral royalties and fuel taxes. On the expenditure side, Le11.27trn (23.50 percent of non-iron ore GDP) in 2021 is forecast as expenditure and net lending. This translated into increased recurrent expenditure and capital expenditure and financing items.

Domestic credit to private sector is projected under the IMF rapid credit facility to rebound from 0.50 percent of non-iron ore GDP in 2020 to 22.80 percent in 2021. The trend of domestic credit to private sector over the years has been low with average about 20 percent. The lending rates charged by banks will remain relatively high with potential adverse implications for investment, consumption and growth. The liquidity conditions in the money market moved in tandem with interest rates and it is expected to provide reprieve for private sector credit to support growth. The banking sector is expected to remain sound and stable as reflected in recent improvements in key financial soundness indicators, underpinned by enhanced regulatory and supervisory regimes, though NPLs ratio remained above the prudential threshold. But continued high lending rates will likely limit the growth in bank lending with potential adverse implications for the growth in investment, consumption and GDP. Over the medium term, any desired switch in bank assets towards private sector credit will likely reduce banks' measured capital and liquidity ratios [since treasury bills are assumed to be risk free and fully liquid unlike private sectors]. This will require further improvements in bank supervision, deepening financial markets and bolstering financial stability measures.

STATISTICAL APPENDICES

Appendix 1: Global Economic Outlook

	World	Proj W	Adv Econs	Proj Aes	EURO AREA	Proj EA	EMDES	Proj EMDES

2018	3.6		2.2		1.9		4.5	
2019	2.9		1.6		1.3		3.7	
2020	-3.2	-3.2	-4.60	4.60	-6.5	-6.5	-2.1	-2.1
2021		6.0		5.6		4.6		6.3
2022		4.9		4.4		4.3		5.2

Source: International Monetary Fund, World Economic Outlook, Washington DC, July, 2021.

Appendix 2: Commodity Price Indexes

COMMODITY PRICES	**NOMINAL U.S DOLLARS (2010=100)**			
Years	2018	2019	2020	2021-Est
Energy	87	76	51.9	70.10
Agriculture	86.7	83.3	87.1	98.90
Minerals and Metals	82.5	78.4	79.1	103.20

Source: WB Commodity Market Outlook April, 2021

Appendix 3: Financial Soundness Indicators

	Dec 2018	Dec 2019	Dec 2020
Regulatory capital to risk weighted assets	38.4	41.7	39.8
Non-performing loans ratio	12.1	16.8	12.2
Return on Assets	6.0	6.1	6.1
Return on Equity	28.6	26.1	26.7

Liquid assets to total assets	66.8	68.4	73.4
Cash ratio	17.6	17.7	20.7
Aggregate net open position in foreign exchange to capital	-12.8	-1.8	-7.5

Source: BSL

Appendix 4: Selected Macroeconomic Indicators for Sierra Leone

	Dec 2018	Dec 2019	Dec 2020
364-Day T-Bills	23.2	25.1	10.5
Interbank rate	16.9	18.6	10.5
Standing Lending Facility rate	20.5	20.5	19.0
Standing Deposit Facility rate	13.5	13.5	10.0
Monetary Policy Rate	16.5	16.5	15.0
Savings deposit rate	2.4	2.9	2.6
Inflation rate (Consumer prices-end of period)	14.2	13.9	12.6
Public debt	69.1	71.8	72.9
GDP at constant prices	3.5	5.5	-2.2

Source: BSL, Sierra Leonean authorities; and Fund staff estimates and projections