BANK OF SIERRA LEONE

MONETARY POLICY REPORT

JUNE 2022

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ACRONYMS

AE	Advanced Economies
AfDB	African Development Bank
BIS	Bank for International Settlement
BOP	Balance of Payments
BSL	Bank of Sierra Leone
CAELS	Capital, Assets, Earnings, Liquidity, Solvency
CAR	Capital Adequacy Ratio
CFC	Customers Foreign Currency
CIEA	Composite Index of Economic Activities
CPI	Consumer Price Index
CRR	Cash Reserve Requirement
dmt	Dry Metric Tons
ECB	European Central Bank
ECF	Extended Credit Facility
ECOWAS	Economic Community of West African States
EMDEs	Emerging Market and Developing Economies
FSIs	Financial Soundness Indicators
FX	Foreign Exchange
GDP	Gross Domestic Product
GFER	Gross Foreign Exchange Reserves
GoSL	Government of Sierra Leone
GST	Goods and Services Tax
HIPC	Heavily Indebted Poor Countries
IMF	International Monetary Fund
M2	Broad Money
MoF	Ministry of Finance
MPC	Monetary Policy Committee
MPR	Monetary Policy Rate
NDA	Net Domestic Assets
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Assets
NPLs	Non-Performing Loans
ODCs	Other Depository Corporations
OIN	Other Items Net
OMO	Open Market Operations
OPEC	Organization of the Petroleum Exporting Countries
Q1	First Quarter
Q2	Second Quarter
Q3	Third Quarter
Q4	Fourth Quarter
QM	Quasi Money
QAERP	Quick Action Economic Response Programme
REER	Real Effective Exchange Rate
RM	Reserve Money
ROA	Return on Assets
ROE	Return on Equity
SDF	Standing Deposit Facility
SLF	Standing Lending Facility
Stats SL	Statistics Sierra Leone
T-bills	Treasury Bills
WB	World Bank
WEO	World Economic Outlook
WTI	West Texas Intermediate

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The Report

The June 2022 edition of the BSL Monetary Policy Report present an assessment of global and domestic economic developments, mainly during the first quarter of 2022. The report also assesses current developments in the second quarter of 2022 for which data is available, as well as near-term prospects, with a view of implementing appropriate monetary policy consistent with the Bank's policy objectives.

BSL Monetary Policy Objectives

The primary objective of the Bank of Sierra Leone is to achieve and maintain overall price stability in the Sierra Leone economy. However, the Bank's mandate encompasses other important goals, including the stability of the financial system and financial market development, as well as supporting the general economic policy of the government to enhance overall macroeconomic stability.[1]

Monetary Policy Strategy

The BSL is the sole monetary authority in Sierra Leone with a statutory operational independence to conduct monetary policy in the country. The Bank uses appropriate policy instruments to achieve its stated objectives. They include, the Monetary Policy Rate, Open Market Operations (OMOs), Standing Lending and Deposit Facilities, Foreign Exchange Operations, and Cash Reserves Requirement.

Monetary Policy Process

The monetary policy of the Bank is formulated by the Monetary Policy Committee (MPC), which is a statutorily constituted body of seven members. The MPC includes the Governor of the Bank (who serves as the chairperson), Deputy Governor for Monetary Policy, Deputy Governor for Financial Stability, and Four other experts with relevant professional experience in monetary policy and financial market operations nominated by the Governor and approved by the Board of Directors of the BSL. The MPC meets every quarter to assess recent global and domestic economic developments, as well as near-to-medium term prospects and inflation risks. Based on these assessments, a policy decision is made, mainly using the Monetary Policy Rate (MPR) to signal the Bank's monetary policy stance. During deliberations in the MPC meeting, each member proposes a preferred MPR decision supported by underlying reasons. Final decision takes place by vote, with the chairman having the deciding vote in the occurrence of a tie. The final decision is then published in a monetary policy statement on the Bank's website, within forty-eight hours after the MPC meeting. In addition, the Governor and other authorized staff engage the public from time to time to explain the Bank's policy decisions and to clarify emerging economic issues, especially those affecting the conduct of monetary and exchange rate policies, among others.

[1] *Section 7.A of the new BSL Act 2019 states: "(1) the objective of the Bank shall be to achieve and maintain price stability. (2) Without prejudice to subsection (1) the Bank shall contribute to fostering and maintaining a stable financial system. (3) Without prejudice to the attainment of the previous two objectives, the Bank shall support the general economic policy of the Government.*

1. EXECUTIVE SUMMARY

Global economic prospects have deteriorated largely on account of Russia's invasion of Ukraine, and further exacerbated by the economic sanctions imposed on Russia by some advanced economies. Furthermore, the frequent and wide ranging lockdown measures adopted in China to contain the spread of COVID-19, particularly in the manufacturing hubs, have slowed down economic activity in those areas and posed constrains for global supply chain. In addition, the high, broader and more persistent price pressures have led to tightening of monetary policy in many advanced economies including the USA, UK and Canada. China continues to maintain accommodated monetary policy. As a result, global growth forecast for 2022 has been downgraded to 3.6 percent in 2022 (IMF WEO April 2022 edition), about 0.8 percent lower than the previous forecast in the WEO January 2022 edition. The downgrade largely reflects the direct impact of the Russia-Ukraine, and the associated global spillovers.

Global inflation has been accelerated by the surge in global commodity prices which increased to historical levels in 2022Q1, mainly underpinned by the war in Ukraine, coupled with disruptions to supply conditions in other key producing countries. These global developments could spill over to small open economies including Sierra Leone through trade, financial inflows and exchange rate channels.

Domestic economic activities recovered by more than expected in 2021, with real GDP growth upgraded to 3.2 percent in 2021, from 2.9 percent earlier projected. The upward revision largely reflected higher than expected performance in the agriculture, mining, manufacturing and services sectors. However, growth prospects for 2022 have been downgraded from 6.0 percent in the earlier projection to 3.6 percent. The downgrade mainly reflects the effects of the Russia-Ukraine war, rising energy and food prices as well as the lingering effects of COVID-19 pandemic. Moreover, the high frequency indicator of economic activity (CIEA) estimates produced by Staff showed that economic activities contracted by 2.01 percent in 2022Q1, compared to a growth of 1.32 percent in 2021Q4.

Inflationary pressures remained elevated in 2022Q1 and through to May 2022. Headline inflation (year-on-year) increased from 17.94 percent in December 2021 to 22.06 percent in March 2022, and further to 24.87 percent in May 2022. The increase in inflation was reflected in both food and non-food inflation. Headline inflation is forecast to reach 26.17 percent by end 2022Q2 and 27.67 percent by end 2022Q3. Risks to the forecast are tilted to the upside due to external factors such as the rising global energy and food prices, global supply chain disruptions, the impact of the Russia war and the economic sanctions on Russia. In addition, the persistent exchange rate depreciation could have pass-through effect on domestic prices and cause inflationary pressures.

On the external sector, the trade deficit narrowed during the quarter, mainly on account of higher receipts from iron ore, rutile and diamond exports, which outweighed the increase in imports. The stock of external reserves of the BSL declined in 2022Q1, reflecting increased payments relative to receipts into the reserves, but was enough to cover about 4.9 months of import of goods and services. Exchange rate pressures persisted in the review period, as all the foreign exchange market segments recorded high exchange rate depreciation in 2022Q1 and in May 2022.

The fiscal position deteriorated in 2022Q1, after recording a surplus in the fourth quarter of 2021. The deterioration was on account of the decline in government revenues which was higher than the decline in government expenditures during the review period.

Monetary aggregates recorded mixed trends during the review period, as Reserve Money (RM) contracted while Broad Money (M2) expanded. The contraction in RM reflected a decline in currency issued and Banks's reserves, while M2 growth was mainly on account of increase in the claims on government by both the BSL and commercial banks.

The yields on government securities exhibited mixed trends, with the yield on 364-day Treasury-bills increasing to 24.95 percent in March 2022, and further to 25.04 percent in May 2022 reflecting in part the risk premium. The yields on 182-day Treasury-bills remained broadly the same at 13.21 percent due to reduced demand, while the demand for 91-day Treasury-bills remained subdued due to the high inflation.

The banking sector continues to be relatively stable as the sector remains well capitalized, liquid and profitable. Although the Non-performing Loans (NPLs) decreased slightly in 2022Q1, it remained above the 10 percent regulatory limit. However, the high NPL ratio poses challenges for bank intermediation and could undermine private sector growth and development.

The rest of the report is structured as follows. The second section analyses recent global economic developments including global growth, global inflation, commodity prices and their implications for the Sierra Leone economy. The third section reviews domestic economic developments and outlook. Finally, the fourth section covers the conclusion and decision of the Monetary Policy Committee in June 2022.

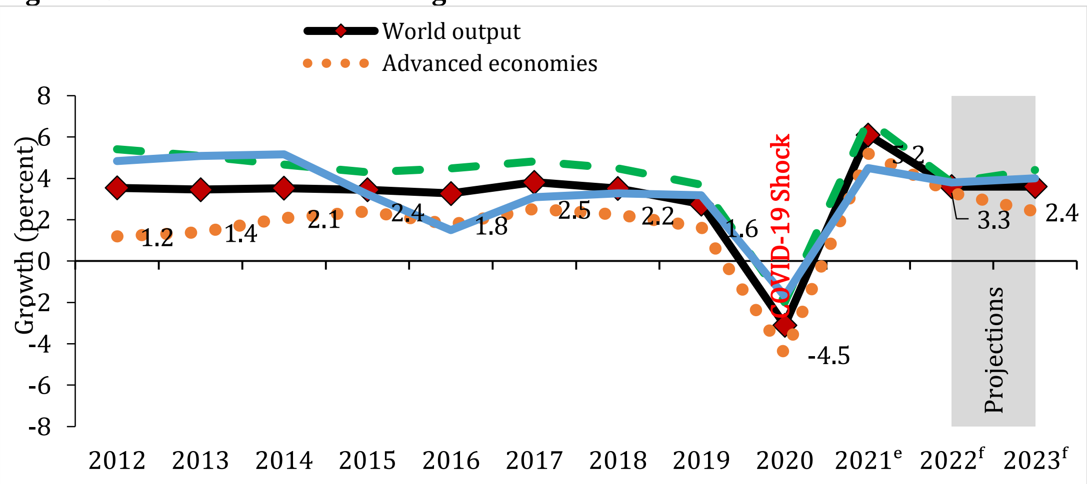
2. GLOBAL ECONOMIC DEVELOPMENTS AND PROSPECTS

2.1 Global Output

Global output slowed, mainly due to the Russian-Ukraine war and new COVID-19 related lockdowns in China after recovering considerably in 2021. These overlapping crises, reinforced by the backlash of sanctions against Russia, created huge macroeconomic imbalances for several countries that weighed heavily on the global economic recovery. This situation has exacerbated supply bottlenecks and inflationary pressures, as well as subdued global growth. In effect, the IMF has further downgraded its January 2022 forecast for global growth to 3.6 percent[2] from 4.1 percent[3]. This reflects forecast downgrades for this year across most major global economies including the United States, China, Euro Area, Japan, Russia and India.

Looking ahead, global economic prospects point to subdued economic activities in the near-to-medium term, as the global growth forecast for 2023 was also revised downwards. Risks to growth outlook largely remain to the downside including, the worsening Russian-Ukraine war, COVID-19 dynamics, worsening supply chain bottlenecks, higher and increased volatility in commodity prices, rising inflationary pressures, narrowing fiscal space and withdrawal of monetary policy stimulus in most economies. Figure 1 depicts the trends in global and regional real GDP growth.

Figure 1: Trends in Global and Regional Real GDP Growth Rates



Source: IMF World Economic Outlook, April 2022; Note: ***e*** =estimate and ***f*** =forecast

[2] IMF World Economic Outlook (WEO), April 2022
[3] IMF World Economic Outlook (WEO), January 2022 update

2.1.1 Advanced and Emerging Markets Economies

Prospects for economic growth dampened across advanced and emerging market economies. Growth forecasts for the two groups in 2022 were revised downwards to 3.3 percent and 3.8 percent, compared with 3.9 percent and 4.8 percent respectively, in the IMF outlook in January 2022. Surging inflation and tightening monetary policy is weighing heavily on economic activities in advanced economies. Consequently, 2022 growth projections for the United States and Euro Area were further downgraded by 0.3 and 1.1 percentage points respectively.

The projected slowdown in emerging markets and developing economies reflects weaker prospects for major economies in the group. New COVID-related lockdowns, downturn in construction sector activities, and cooling exports are affecting economic activities in China. In India, weak industrial production and consumer spending due to soaring price pressures are weighing on economic outcomes. Russia, which is another major emerging market economy, is expected to record a severe recession this year following the numerous sanctions imposed on Moscow for the invasion of Ukraine. Consequently, growth forecast for China, India and Russia were revised downward by 0.4, 0.8, and 11.3 percentage points, respectively. Going forward, expected further policy rate hikes in major advanced economies (especially the United States) in response to rising inflationary pressures, as well as the possible protraction of the Russia-Ukraine crisis are major downside risks to the growth outlook in the groups.

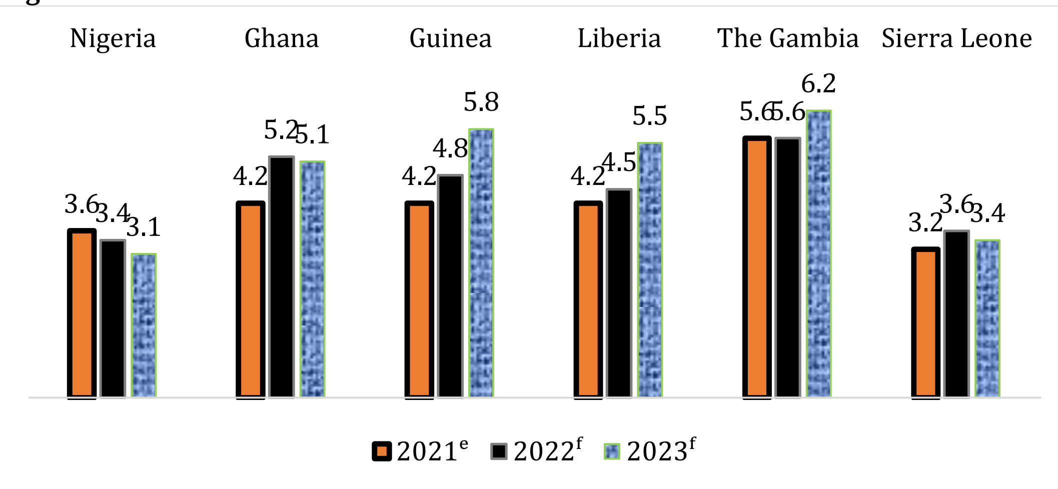
2.1.2 Sub-Saharan Africa (SSA)

The stronger-than-expected economic recovery in Sub-Saharan Africa during the second half of 2021 has been greatly derailed by the onset of the Russian-Ukraine conflict. The region is, thus, expected to record moderate growth of 3.8 percent in 2022, relative to the 4.5 percent growth in 2021. Worsening supply chain conditions and soaring food and energy prices, mainly due to the escalating Russian-Ukraine war has presented major challenges for economic management in the region with limited space for policy response. A major risk to the outlook of the region is rising debt-to-GDP ratios, placing many countries in debt distress risks. Social tensions due to rising unemployment and deteriorating living conditions could also adversely affect economic prospects in the region.

2.1.3 West African Monetary Zone (WAMZ)

WAMZ member economies rely heavily on the importation of fuel and food, whose prices have being surging since the outbreak of the war in Ukraine. Although the biggest economy in the bloc may be benefiting from higher crude oil prices, the net economic impact in the bloc could be negative. This is evident in the downward revision of 2022 growth projection for Ghana (by 0.3 percentage points), Sierra Leone (2.4 percentage points), Guinea (1.3 percentage points), Liberia (0.2 percentage points) and The Gambia (0.4 percentage points), while Nigeria's growth projection was revised upwards by 0.7 percentage point. Looking ahead, near-term economic prospects in the bloc remain clouded with high uncertainty. Growth risks remain largely on the downside mainly as a result of the war in Ukraine, COVID-19 legacy effects, rising debt, weakening currencies, surging energy and food prices fueling inflationary pressures in the bloc. **Figure 2** depicts growth in the **WAMZ economies.**

Figure 2: Trends in Real GDP Growth in the WAMZ



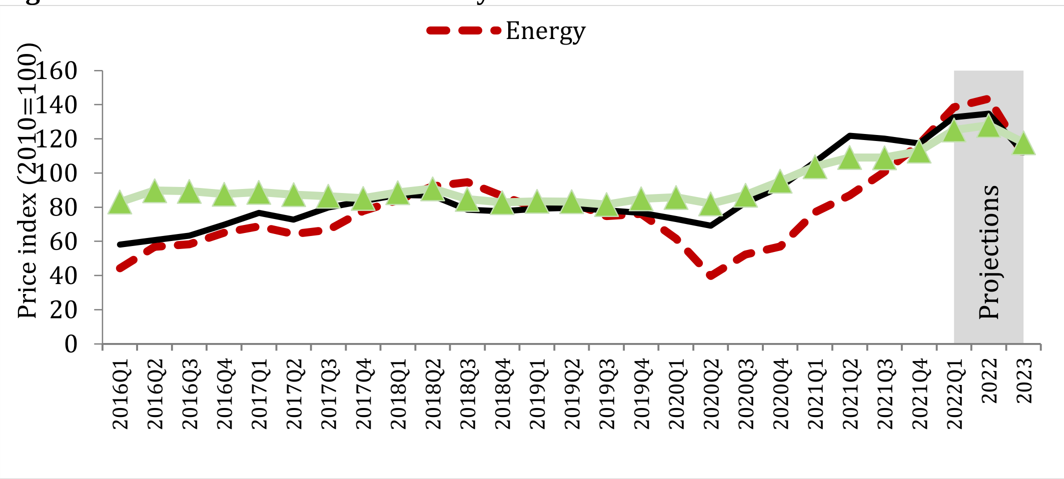
Source: IMF WEO , April 2022; Note: e =estimate and f =forecast

2.2 Commodity Prices and Inflation

2.2.1 Global Commodity Prices

Global commodity prices surged to historical levels in 2022Q1, mainly underpinned by the war in Ukraine, coupled with poor supply conditions in other key producing countries. Energy prices recorded the steepest increase of 18.49 percent to an index of 138.54 in 2022Q1, underscored by the dominant role of Russia in the export market of energy products. Metals and Agriculture prices increased by 12.94 percent and 10.90 percent to indices of 132.56 and 125.17 in 2022Q1, respectively. Prices are expected to peak by the end of 2022, and could remain significantly higher in the short-to-medium term. Looking ahead, global commodity price dynamics will depend largely on the duration of the war in Ukraine and how fast alternative supply sources can be boosted to match the increasing demand amidst supply constraint (**see Figure 3**).

Figure 3: Trends in Global Commodity Price Indices

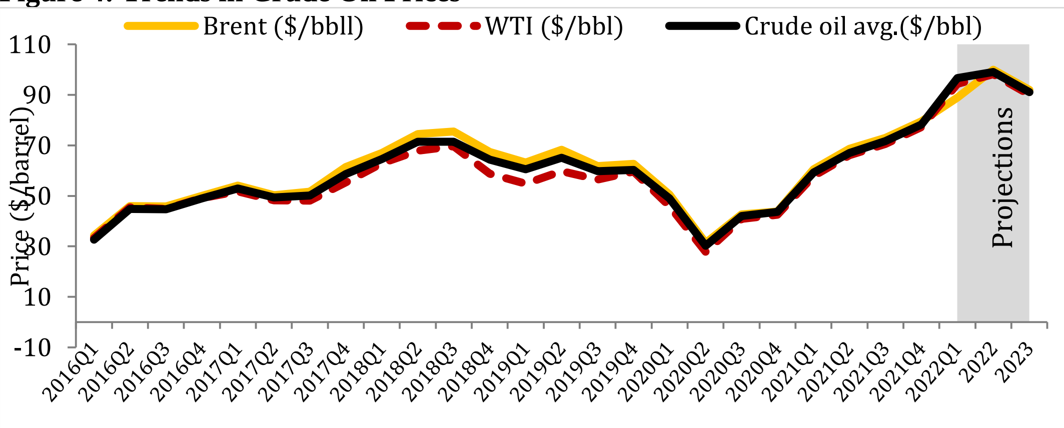


Source: World Bank Commodity Market Outlook database, February 2022

Crude Oil Prices

The Ukraine war has intensified the pre-existing surge in crude oil prices in 2022Q1. Crude oil was recording significant price gains before the Russia-Ukraine crisis, but prices increased more sharply at the onset of the war in February 2022. Both Brent and WTI crude prices surged by 11.77 percent and 22.12 percent selling at US$88.94/bbl and US$94.45/bbl in 2022Q1. Crude oil is projected to average US$99.10/bbl in 2022, the highest price since 2008. Though prices are expected to recede somewhat in 2023, they could remain above pre-war levels especially if geopolitical tensions escalate.

Figure 4: Trends in Crude Oil Prices

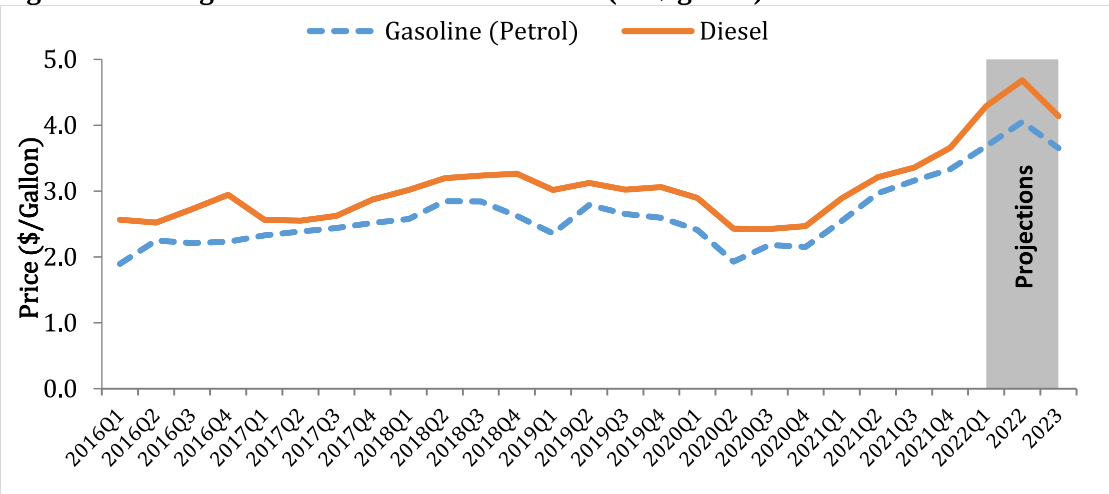


Source: World Bank Commodity Market Outlook database, June 2022

Petroleum Products (Retail Prices)

Reflecting the surge in crude oil prices, the retail global prices for both petrol and diesel increased by 10.63 percent and 17.13 percent to US$3.68/gallon and US$4.29/gallon in 2022Q1, respectively. Retail prices are expected to strengthen in 2022 on average before receding slightly in 2023, but may remain above pre-existing levels in the medium term.

Figure 5: Average Prices of Petroleum Products (US$/gallon)

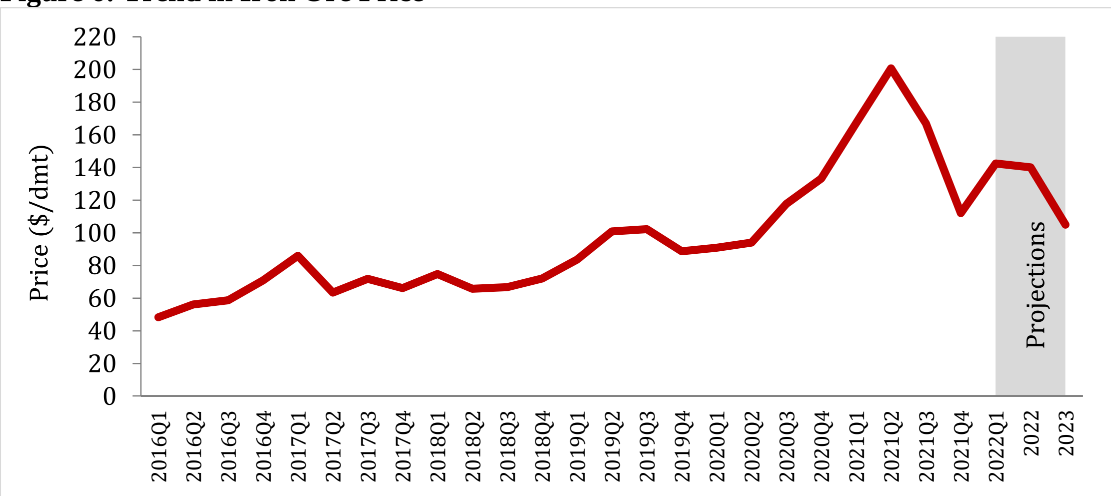


Source: U.S. Energy Information Administration, EIA (June, 2022)

Iron Ore Price

Iron ore prices made some gains in 2022Q1, mainly on account of Russia's importance in the commodity market coupled with higher extraction and transportation cost due to rising fuel prices. Though the projected average price of US$140.00/dmt in 2022 is significantly lower than in 2021, it remains above pre-pandemic levels. However, prices are tipped to drop in 2023 contingent on weakening demand in China and inventory build-ups in Australia and Brazil.

Figure 6: Trend in Iron Ore Price



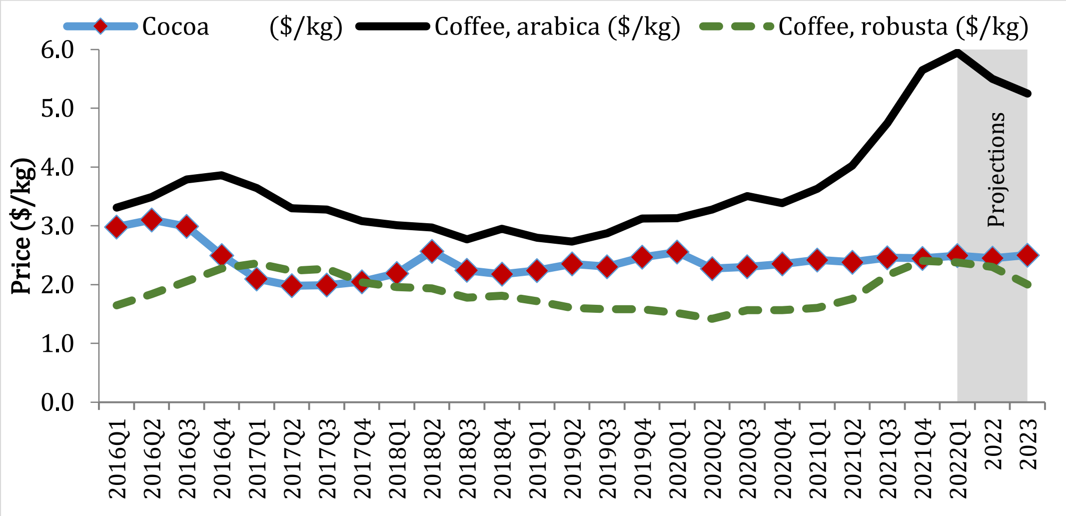
Source: World Bank Commodity Market Outlook database, June 2022

Cocoa and Coffee Prices

In 2022Q1, Cocoa and Robusta coffee prices remain relatively stable, amid rising global economic uncertainties. Cocoa was selling at an average price of US$2.49/kg in 2022Q1, compared with US$2.45/kg in 2021Q4. Similarly, Robusta coffee was selling at US$2.38/kg in 2022Q1, compared with US$2.41/kg. However, Arabic coffee price rose further averaging

US$5.95/kg in 2022Q1, from US$5.64/kg in 2021Q4. The increase in Arabica coffee price reflects tight supply conditions as output from Brazil (the world's largest producer) declined. Prices are projected to revolve around current levels in the near-to-medium term.

Figure 7: Trends in Cocoa and Coffee Prices

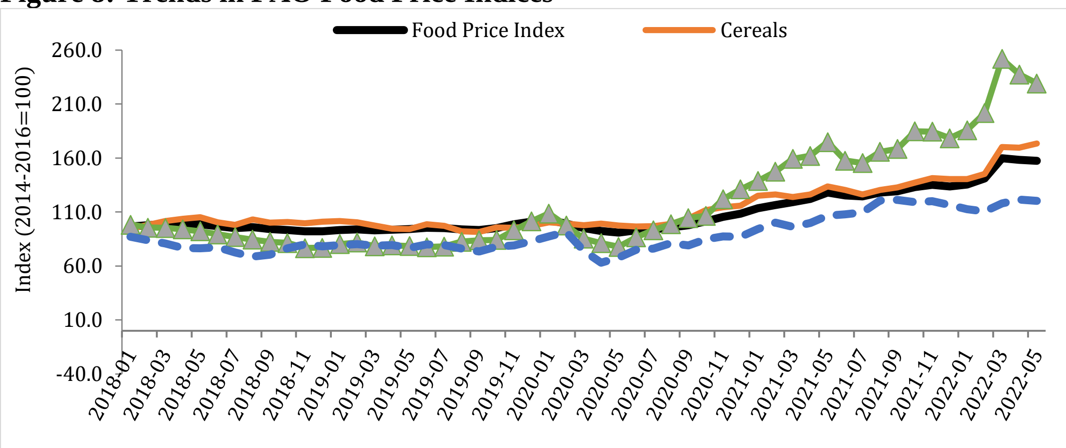


Source: World Bank Commodity Market Outlook database, June 2022

Food

Based on the FAO food price index reports, average food price increased significantly, reaching a historical level with an index of 159.7 in March 2022, from 133.7 in December 2021. However, it receded in April (158.3) and May (157.4) 2022. Vegetable oils and cereals recorded high increases mainly on account of the war in Ukraine and supply restrictions in some palm oil producing countries.

Figure 8: Trends in FAO Food Price Indices

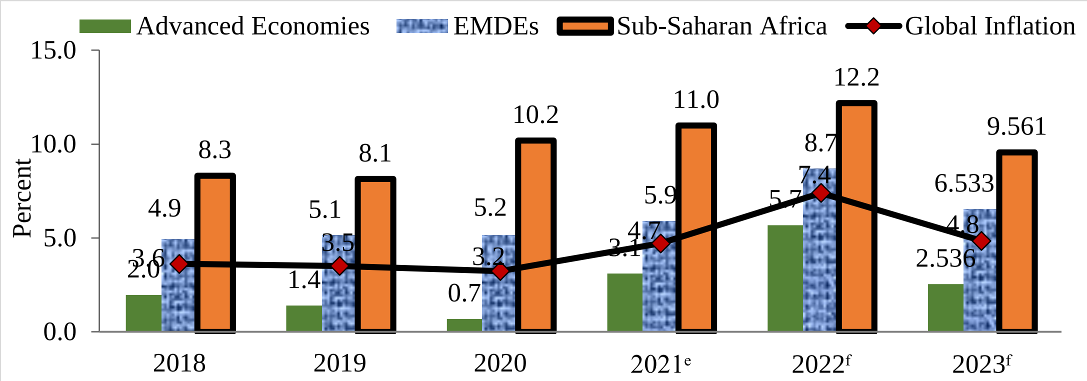


Source: FAO food price index database, May 2022

2.2.2 Global Inflation

Pre-existing global inflationary pressures have been exacerbated by the Russian-Ukraine war as reflected in the upward movement in commodity prices and worsening supply disruptions. Consequently, the IMF in its World Economic Outlook (WEO) in April 2022 projected global inflation this year at 7.4 percent, representing an upward revision of 3.3 percentage points. Global inflation is anticipated to moderate in 2023, but could remain above targets in most economies. **Figure 9** depicts the trends in global and regional inflation

Figure 9: Trends in Global and Regional Inflation Rates



Data source: IMF, World Economic Outlook, April 2022

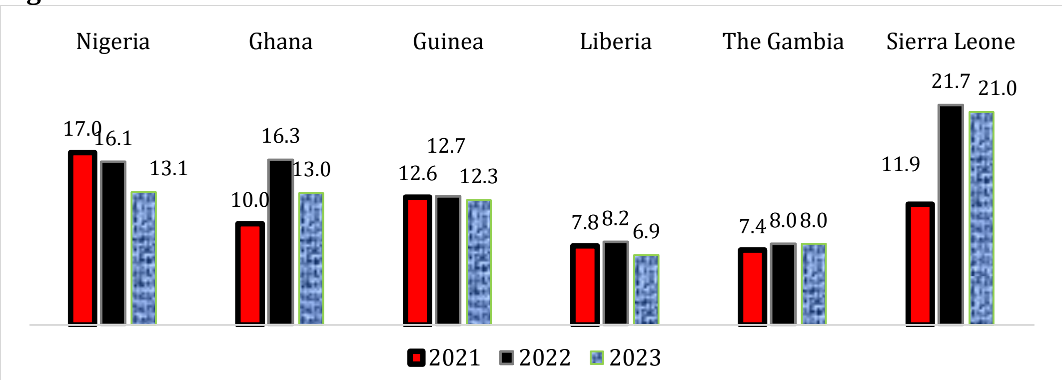
Sub-Saharan Africa Inflation

Most SSA countries are net commodity importers. Hence, the surge in commodity prices on the back of the Ukraine war is worsening inflationary pressures in the region. Inflation in the region is expected to remain elevated at 12.2 percent and 9.6 percent in 2022 and 2023, respectively. Risks to inflation outlook in the region remained high on the upside and include rising energy and food prices, continued supply chain issues and exchange rate depreciation as advanced economies raise their interest rates.

Inflation in the WAMZ

Inflationary pressures continue to soar in the WAMZ member economies. One of the primary WAMZ performance criteria is single digit inflation for all the six member countries. The current rise in inflationary pressures in the member economies could further delay the implementation of a single currency in the zone as only two out of the six countries is projected to record single digit inflation in 2022-2023(**see Figure 10).**

Figure 10: Trends in Inflation in the WAMZ



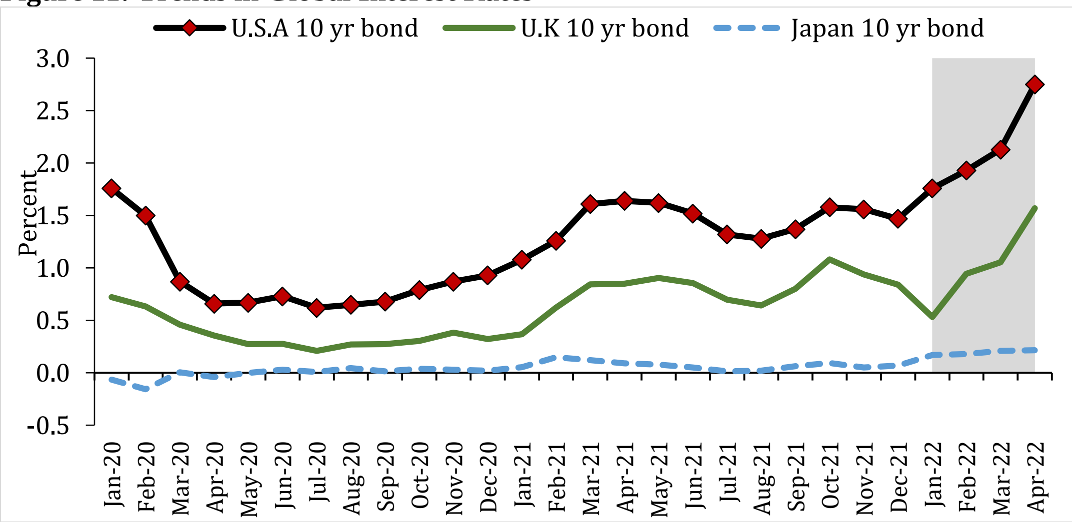
Data source: IMF, World Economic outlook, April 2022

2.3 Monetary Policy and Financial Market Developments

Central Banks around the world have started normalizing monetary policy in response to the rapidly growing inflationary pressures, which have been intensified by the fallout from the war in Ukraine (See **Table 2** in appendix). Most central banks are seen to respond more aggressively than previously anticipated to bring down inflation to near target levels by 2023.

Expected hikes in central banks' policy rates (especially in the United States), coupled with the growing uncertainties being brought about by the war in Ukraine have led to tightening global financial conditions. Consequently, the 10-year sovereign bond yields in the United States, United Kingdom and Japan have risen sharply in the first four months in 2022 (see **Figure 11**).

Figure 11: Trends in Global Interest Rates



Source: FRED (June, 2022)

2.4 Implications for the Outlook of the Sierra Leone Economy

The outbreak of the war in Ukraine has presented further challenges for economic management across the globe. The fallout from the war has led to weakening global economic activities, worsening trade conditions and rising inflationary pressures. These global developments could spill over to small open economies including Sierra Leone through trade, financial inflows and exchange rate developments. Higher fuel and food prices could raise the import bill of the country. Conversely, weak economic activities in China and Europe – two of Sierra Leones major trading partners - could lead to a drop in the country's export. Additionally, tightening global financial conditions could lead to slower financial inflows especially in relation to foreign direct investment (FDI) and Official Development Assistance (ODA). Slower financial inflows could subsequently put pressures on gross foreign exchange reserves, with adverse implications for exchange rate stability. However, firming global prices for the country's main export commodities and improved remittance inflows could help in neutralizing some of these adverse effects.

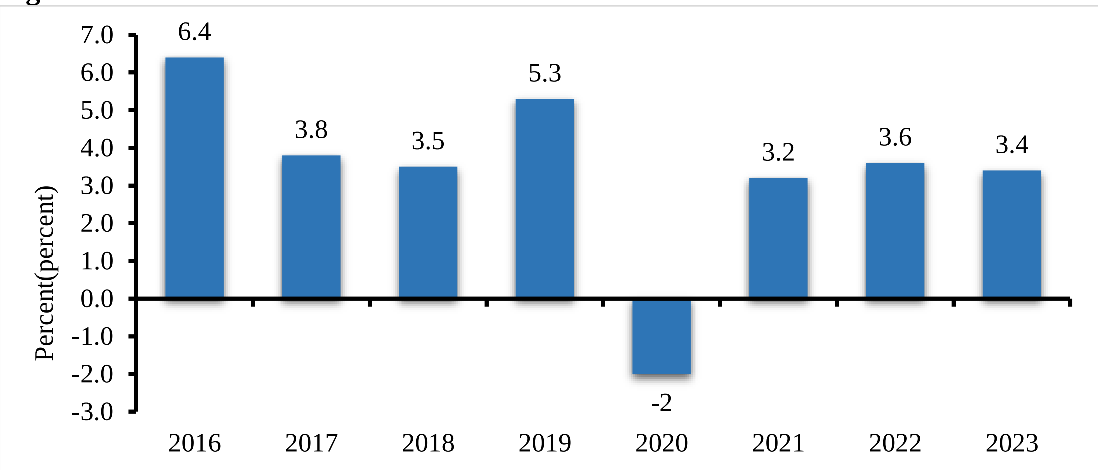
3. DOMESTIC ECONOMIC DEVELOPMENTS

3.1 Real Sector Developments

3.1.1 Real GDP growth

The domestic economy was initially projected to grow at 6.0 percent in 2022, but recent assessment shows a downgrade to 3.6 percent in 2022. The anticipated revised growth was in part explained by the effects of the global uncertainties, renewed challenges and risk from the war in Ukraine and other supply-side shocks. Despite these challenges, diverse policy reforms in other sectors such as agriculture, tourism, trade and services sectors among others could support growth. **Figure 12** shows the real GDP growth rates.

Figure 12: Real GDP Growth Rates

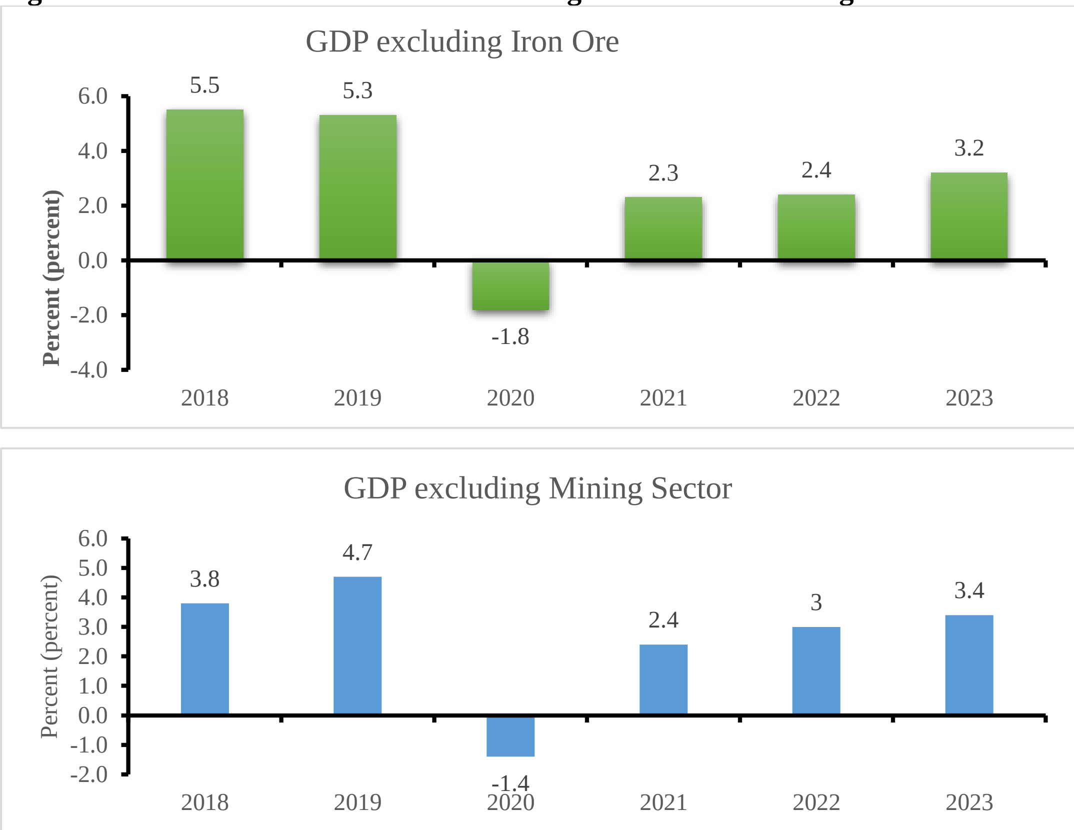


Source: Stats SL & IMF

Excluding the mining sector, real GDP growth is estimated at 3.0 percent in 2022, compared to 2.4 percent in 2021. Real GDP growth excluding iron ore is projected at 2.4 percent in 2022 from 2.3 percent growth in 2021. Figure 13 shows real GDP growth excluding iron ore and mining sector.

Real GDP growth is projected at 3.4 percent in 2023, about 0.2 percentage point lower than the expected growth rate in 2022. The weaker performance in 2023 reflects the uncertainty surrounding the war in Ukraine and the effects on commodity prices and supply constraints.

Figure 13: Real GDP Growth Rates Excluding Iron Ore and Mining Sector



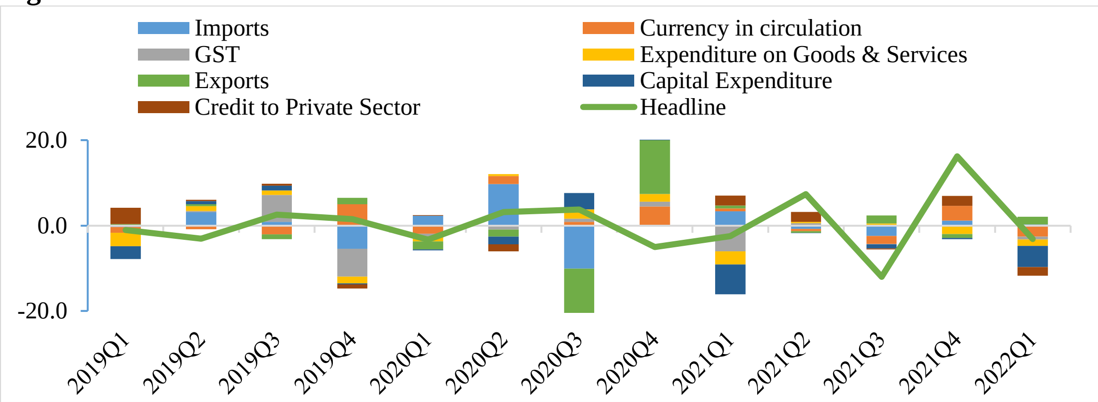
Source: Stats SL & IMF

3.1.2 Composite Index of Economic Activity (CIEA)

The Composite Index of Economic Activity (CIEA) estimates (q/q) produced by BSL Staff showed that economic activities contracted by 2.01 percent in 2022Q1, compared to a growth of 1.32 percent in 2021Q4. The contraction in the estimated growth was partly attributed to the slowdown in all the major high frequency indicators except imports and exports which increase in the review period. Meanwhile, currency in circulation, GST, expenditure on goods and services, capital expenditure and credit to the private sector declined during the review period.

On a year-on year basis, the Composite Index of Economic Activity (CIEA) estimates showed that the economy contracted by 2.77 percent in 2022Q1, compared to a growth of 6.38 percent in 2021Q1. The negative growth was on account of the decline in currency in circulation, GST, expenditure on goods and services, capital expenditure and imports. Whilst, credit to the private sector and exports improved in the reporting period. **Figure 14** shows the quarterly contributions of high frequency indicators to composite index of economic activity.

Figure 14: Contributions to CIEA



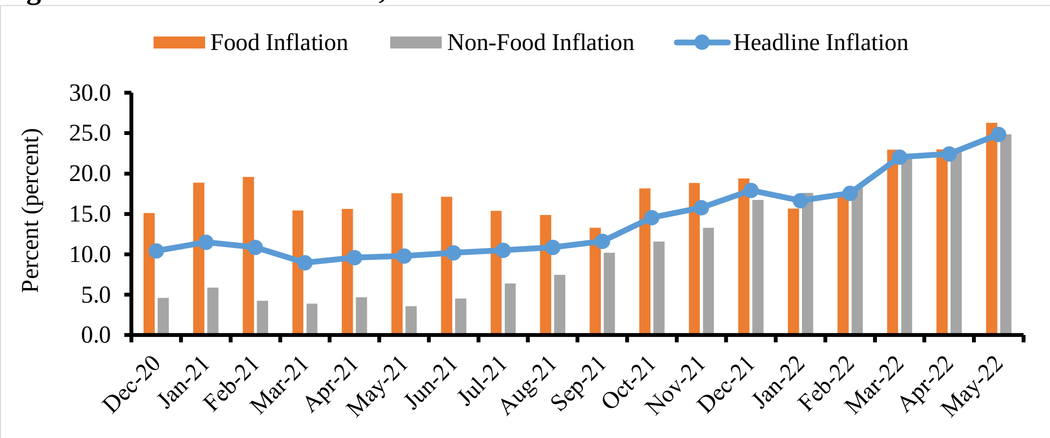
Source: BSL, staff estimation

3.1.3 Inflation Developments

Inflationary pressures remained elevated in 2022Q1 and through to May 2022, partly explained by the supply chain disruptions and surge in international prices of energy and food induced largely by the war in Ukraine. Headline inflation (year-on-year) increased from 17.94 percent in December 2021 to 22.06 percent in March 2022, and further to 24.87 percent in May 2022. The increase in inflation was reflected in both food and non-food inflation.

Food inflation increased from 19.40 percent in December 2021 to 22.96 percent in March 2022, and further to 23.00 percent in May 2022. Similarly, Non-food inflation increased from 16.75 percent in December 2021 to 21.86 percent in March 2022, and further to 24.84 percent in May 2022. **Figure 15** shows headline inflation and the disaggregated components.

Figure 15: Trends in Headline, Food and Non-food Inflation



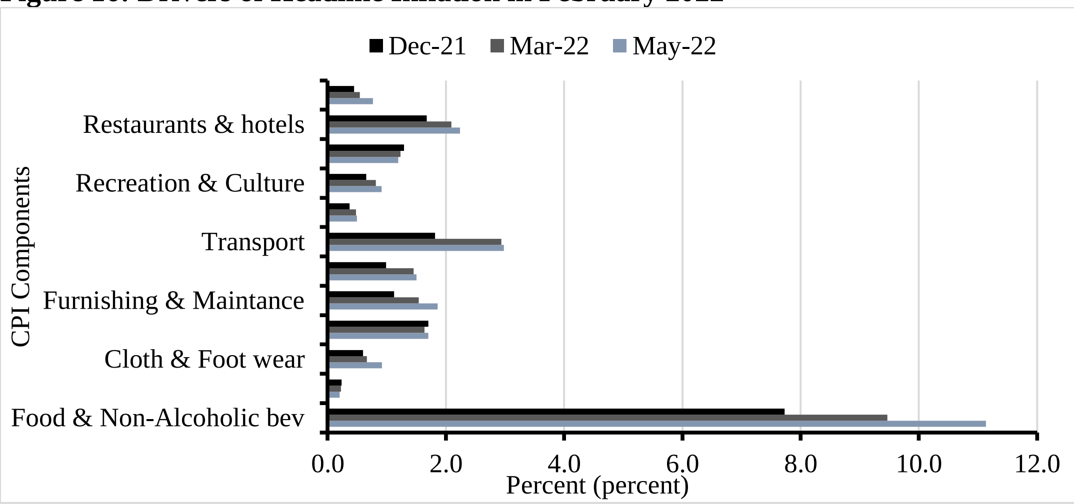
Source: Stats SL

Drivers of Headline Inflation

Key drivers of inflation in May 2022 were: food & non-alcoholic beverages, alcoholic beverage, tobacco & narcotics, clothing & footwear, housing and utilities, furnishing & maintenance, health, recreation & culture, restaurants & hotels, and miscellaneous goods & services.

However, other components in the CPI basket including, communication and restaurant recorded decreases in inflation, while education remained unchanged. **Figure 16** shows the components in the CPI basket contribution to inflation.

Figure 16: Drivers of Headline Inflation in February 2022



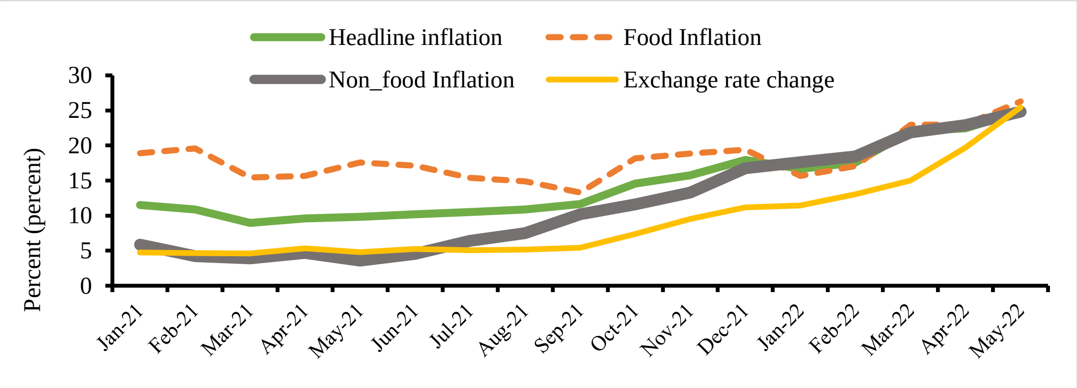
Source: BSL Staff estimates using Stats SL data

On a month-on-month basis, headline inflation moderated to 2.43 percent in May 2022 compared to 4.68 percent in March 2022 and 2.12 percent in December 2021.

Trends in Exchange Rate and Inflation

The headline inflation, food inflation, non-food inflation and exchange rate have exhibited upward trends since 2022Q1, and continued in May 2022. In May 2022, exchange rate depreciation was almost at par with the headline inflation and its main components- food inflation and non-food inflation. The increase in inflation could partly be due with the deprecation of the exchange rate as well as other external factors. **Figure 17** shows headline inflation, food and non-food inflation and exchange rate depreciation.

Figure 17: Inflation Rates and Exchange Rate

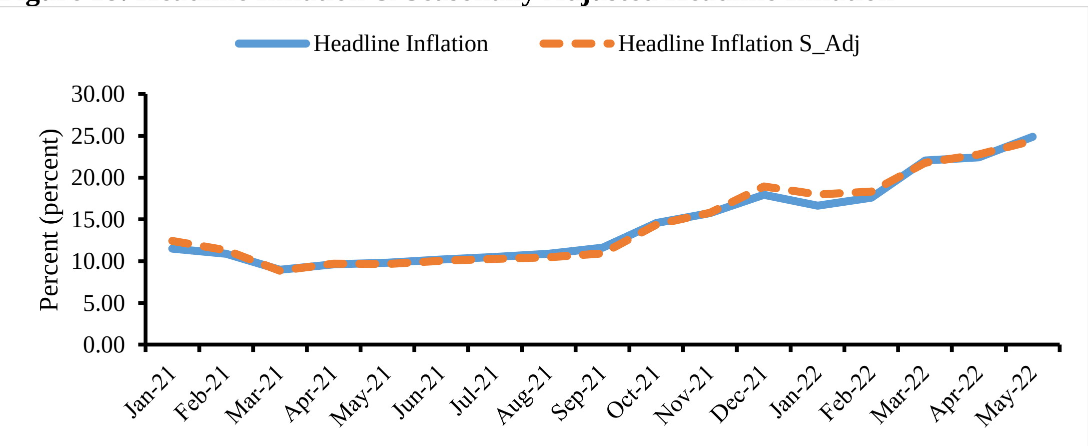


Source: BSL Staff estimates using Stats SL data

Inflation and Seasonally Adjusted Inflation

In **figure 18** below, both headline inflation and seasonally adjusted inflation are moving in the same direction and are at par, reflecting no significant effect of seasonality.

Figure 18: Headline Inflation & Seasonally Adjusted Headline Inflation



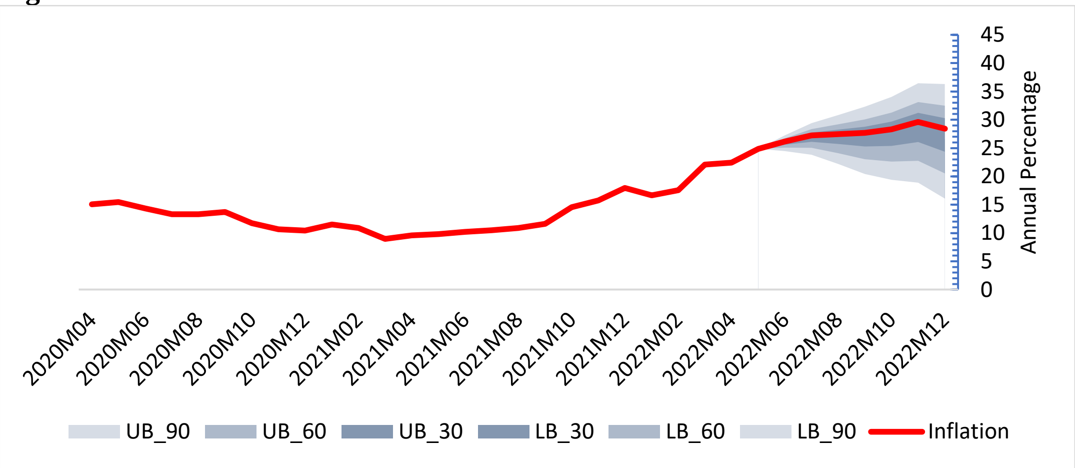
Source: BSL Staff estimates using Stats SL data

3.1.4 Inflation Forecast

The inflation forecast is based on three models namely, ARIMA, ARIMAX and BVAR models. Based on ARIMA model, inflation is projected to rise from 25.8 percent in 2022Q2 to 27.8 percent in 2022Q3, but expected to decrease to 27.2 percent in 2022Q4. The ARIMAX model forecast inflation to reach 25.13 percent in 2022Q2, while the Bayesian Vector Autoregressive (BVAR) model forecast inflation to rise to 26.97 percent in 2022Q2, and further to 27.39 percent in 2022Q3. (**Table 7**). A combined forecast from the three models shows that inflation will rise to 26.17 percent in 2022Q2, 27.67 percent in 2022Q3 and 28.42 percent in 2022Q4.

The inflation Fan Chart indicates a prospect for downside inflationary pressures in the forecast horizon. However, the unfolding global developments, including geopolitical tensions may further heighten risks to inflation outlook.

Figure 19: Inflation Fan Chart



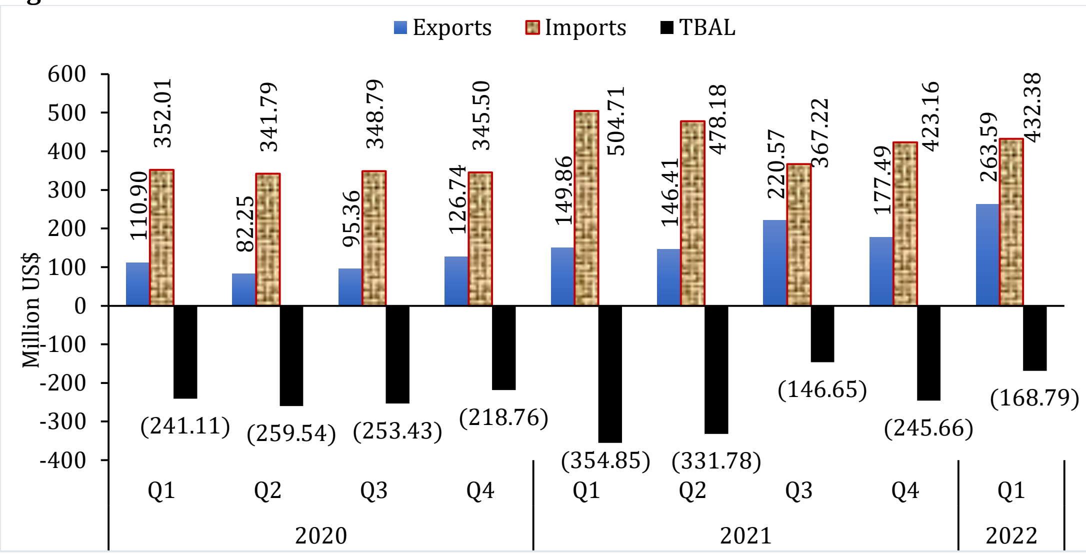
Source: BSL Staff estimates using Eviews

3.2 External Sector Developments

3.2.1 Trade Balance

The trade balance somewhat improved in 2022Q1, as trade deficit narrowed from US$241.11million in 2021Q4 to US$168.79million in 2022Q1. This improvement mainly reflected higher export earnings from iron ore, rutile and diamond during the review period.

Figure 20: International Trade

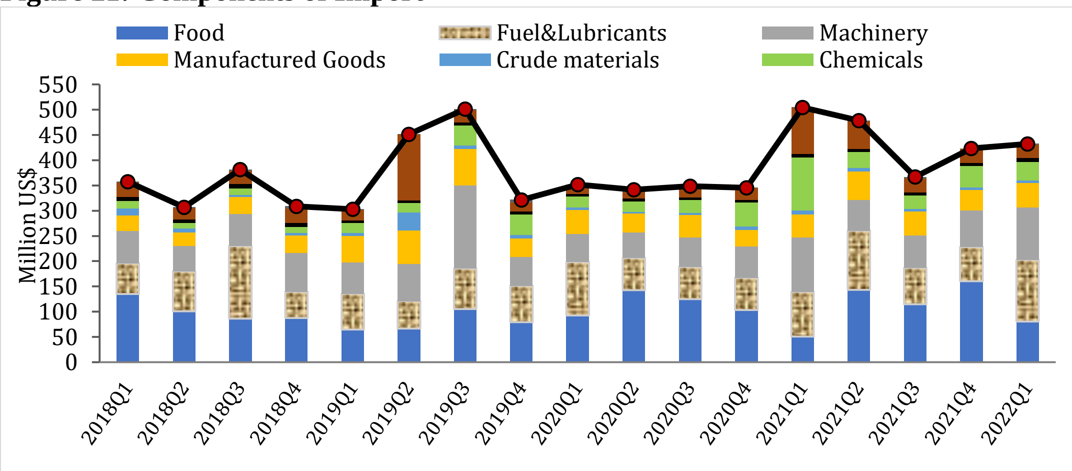


Source: NRA/Customs & BSL

Components of Import

Consistent with increasing global commodities prices and freight cost, the import bill grew by 2.18 percent to US$432.38million in 2022Q1, compared with US$423.16million in the preceding quarter. The growth in import bill was reflected mainly in payment for petroleum products, machinery-transport equipment, and manufactured goods (see **Figure 22**)

Figure 21: Components of Import

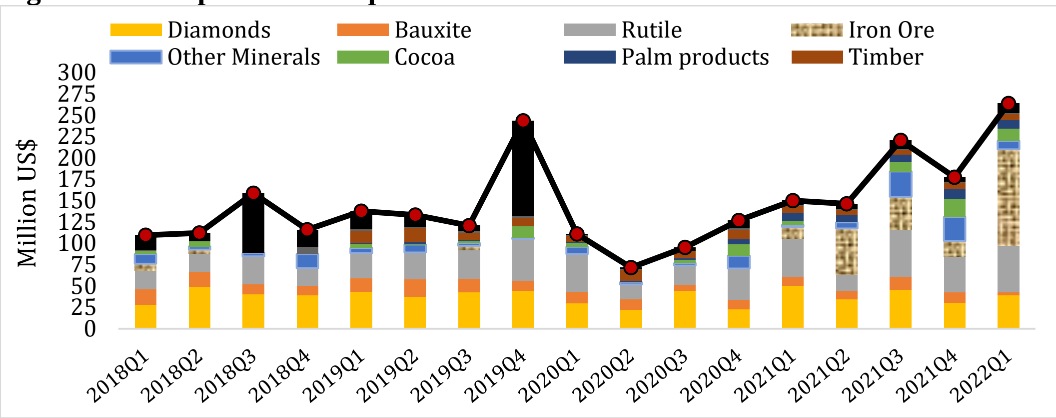


Source: NRA/Customs & BSL

Components of Export

Exports improved significantly in 2022Q1, boosted by increased iron ore, rutile and diamond export earnings due to increases in both prices and volume during the review period. Total export receipts improved to US$263.59million in 2022Q1, compared with US$177.49million and US$149.86million in the preceding and corresponding quarters in 2021, respectively (see **Figure 23**).

Figure 22: Components of Export

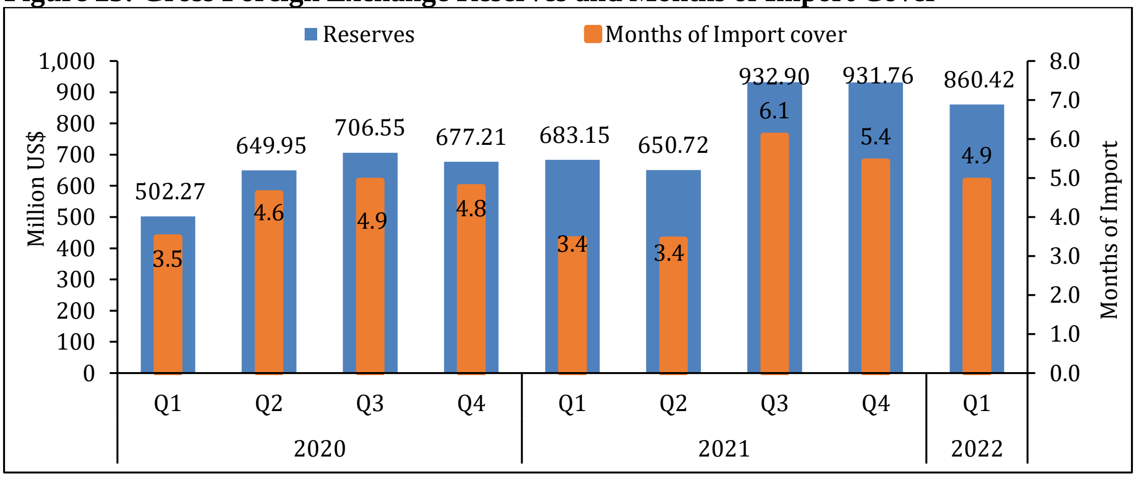


Source: NRA/Customs & BSL

3.2.2 Gross Foreign Exchange Reserves

The stock of gross foreign exchange reserves of the BSL declined from US$931.76million in 2021Q4 to US$860.42million in 2022Q1. In terms of months of import cover, it reduced from 5.4 months of imports in 2021Q4 to 4.9 months of imports in 2022Q1.

Figure 23: Gross Foreign Exchange Reserves and Months of Import Cover

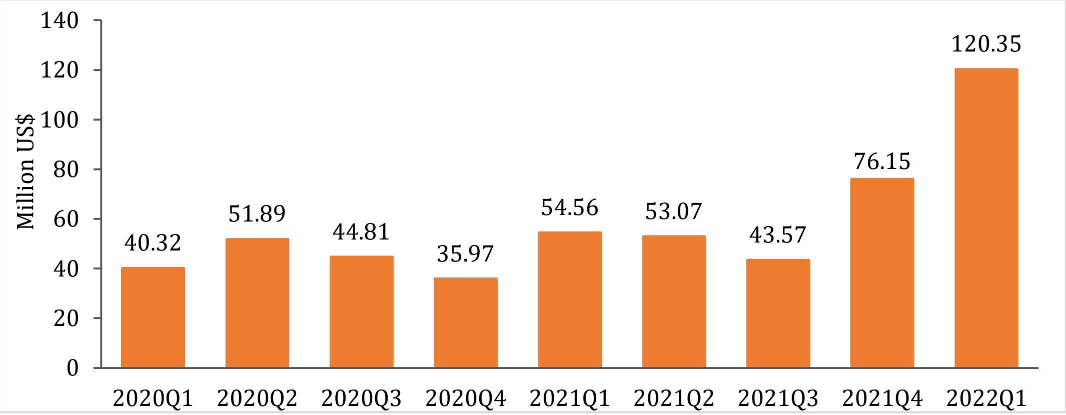


Source: BSL

3.2.3 Diaspora Remittances

Diaspora remittance inflows continued to strengthen in the review period, which could help in neutralizing some of the growing economic challenges in the country. Diaspora remittances increased by 58.05 percent to US$120.35million in 2022Q1, compared to US$76.15million in 2021Q4.

Figure 24: Diaspora Remittances into Sierra Leone

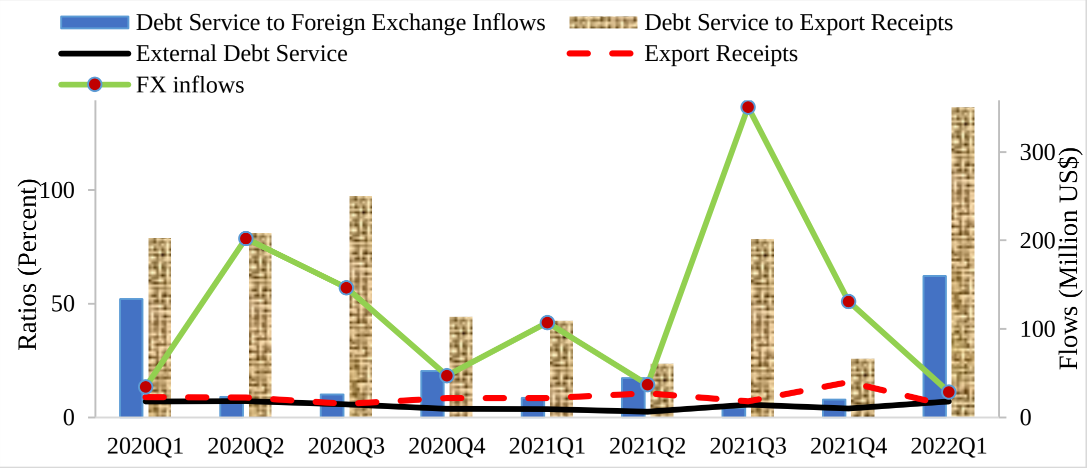


Source: BSL

3.2.4 External Vulnerability Ratios

External debt service payments increased to US$17.89million in 2022Q1, compared with US$10.17million in 2021Q4. Conversely, both foreign exchange (FX) inflows and export receipts decreased significantly in 2022Q1 relative to the preceding and corresponding periods in 2021. Consequently, both external debt service to FX inflows and external debt service to export receipts increased significantly during the review quarter.

Figure 25: External Vulnerability Ratios



Source: BSL

3.2.5 External Sector Outlook

Uncertainties in the external sector have increased significantly on the back of the Russian-Ukraine conflict. The war has worsened global supply conditions and induced significant increases in energy and food prices. This could have adverse effects on the country's trade balance and foreign exchange market. However, high prices for export commodities – including iron ore, rutile and diamonds – combined with growing diaspora remittances could help in attenuating the negative reverberations in the external sector.

3.3 Exchange Rates and Foreign Exchange Market Developments

3.3.1 Exchange Rate Movement

The stability of the exchange rate remained challenged in 2022Q1, given the liquidity constraints that have subsisted from the second half of 2021 and the hike in crude oil prices as well as the increasing cost of freight. This is coming against the backdrop of the global negative supply shock induced by the Russian –Ukrainian crisis.

The pressures on the exchange rate are also coming from increased demand for foreign exchange for the importation of food, petroleum products and other trade related commodities for the rainy season. In addition, the uncertainties in the foreign exchange market remained elevated as the country plans to redenominate its currency, giving rise to some speculative activities in the FX market.

To dampen the pressures on the exchange rate, the Bank of Sierra Leone in April 2022 created two new Special Facilities - a Special Fund for Food to the tune of US$50million and a Special Fund for Oil to the tune of US$36million. This intervention was done to help cushion the liquidity constraints in the foreign exchange market as well as to support the importation of essential goods.

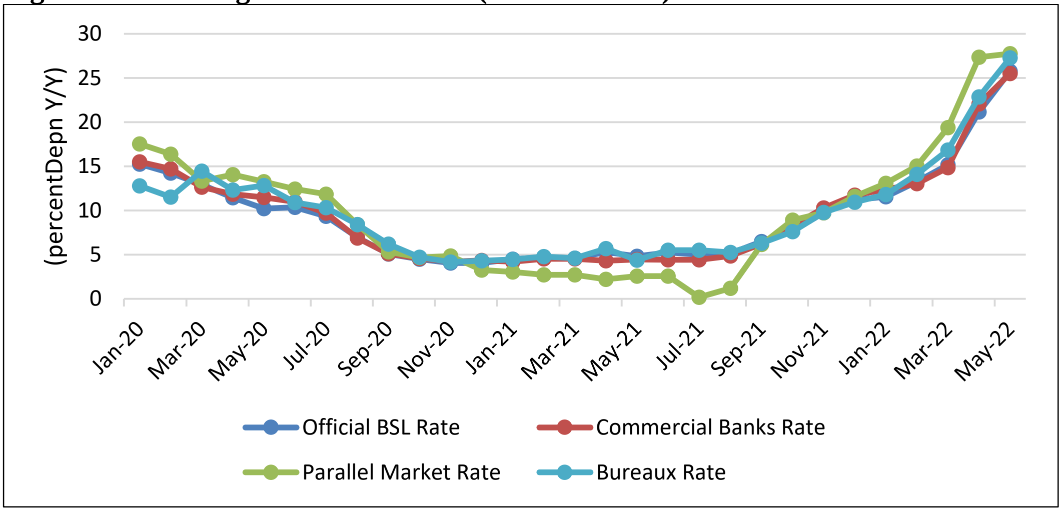
The official BSL exchange rate of the Leone against the US dollar depreciated by 5.20 percent, averaging Le11,568.33/US$1 in 2022Q1 relative to Le10,996.16/US$1 in 2021Q4. It also depreciated by 13.34 percent when compared to Le10,207.07/US$1 in the corresponding quarter of 2021.

The commercial bank's exchange rate depreciated by 4.31 percent, averaging Le11,692.95/US$1 in 2022Q1 relative to Le11,209.55 in 2021Q3. It also depreciated by 13.43 percent when compared to Le10,308.88/US$1 in the corresponding quarter of 2021.

The bureaux rate depreciated by 6.17 percent, averaging to Le11,689.99/US$1 in 2022Q1 from to Le11,010.19/US$1 in 2021Q4. Similarly, it depreciated by 14.26 percent when compared to Le10,231.34/US$1 in the corresponding quarter of 2021.

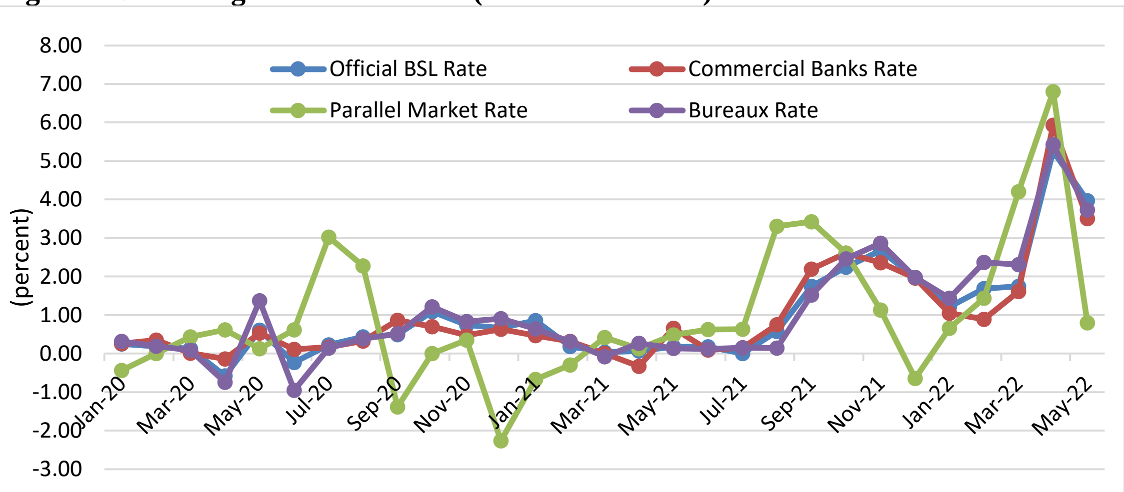
The Parallel market rate depreciated by 2.99 percent, averaging to Le12,010.42/US$1 in 2022Q1, relative to Le11,662.08/US$1 in 2021Q4. It also depreciated by 15.83 percent when compared to Le10,368.58/US$1 in the corresponding quarter of 2021.

Figure 26: Exchange Rate Movement (Year-on-Year)



Source: BSL

Figure 27: Exchange Rate Movement (Month-on-Month)

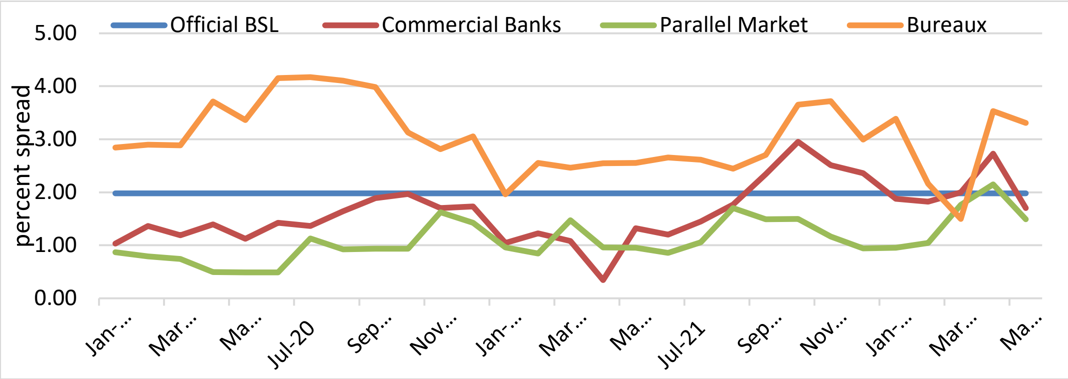


Source: BSL

3.3.2 Exchange Rate Spread in Various Market Segments

The official BSL rate spread remained unchanged at constant at 1.98 percent in May 2022. However, spreads in the commercial banks, bureaus, and parallel market were 1.70 percent, 3.31 percent, and 1.49 percent respectively, as at end May 2022.

Figure 28: Average Monthly percent Spread in the Different Exchange Rate Markets



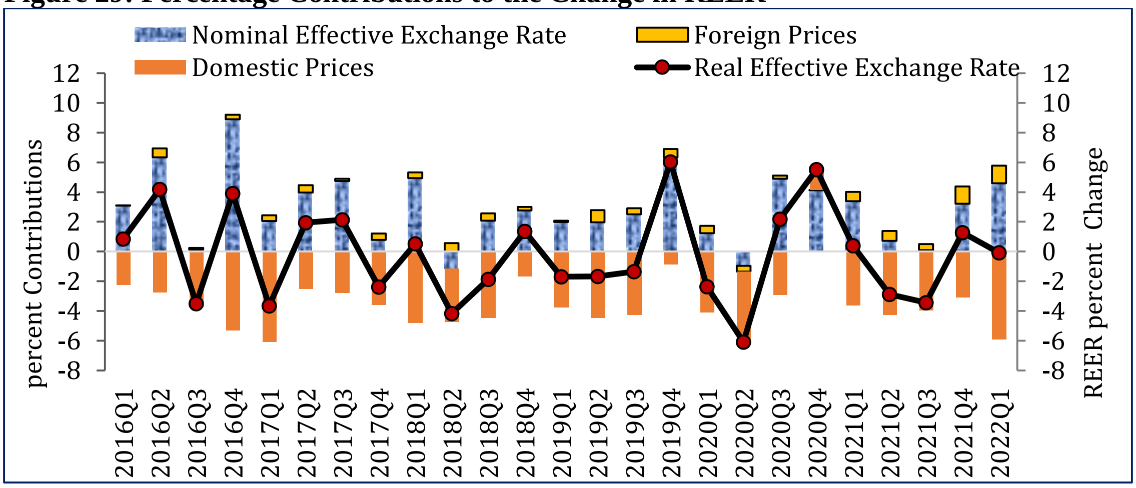
Source: BSL

3.3.3 Effective Exchange Rates

The Nominal Effective Exchange Rate (NEER), which measures the relative strength of the Leone against the currencies of Sierra Leone's trading partners depreciated by 4.70 percent to an index of 313.03 in 2022Q1. Bilaterally, the Leone depreciated against the Chinese RMB by 5.99 percent, US dollar by 5.27 percent, Swiss franc by 5.02 percent, British Pounds by 4.87 percent and Euro by 4.09 percent.

However, the Real Effective Exchange Rate (REER), which measures the competitiveness of Sierra Leone's traded goods relative to those of its trading partners appreciated slightly by 0.08 percent to an index of 97.24 points in 2022Q1. The appreciation was mainly on account of significant increase in domestic prices relative to foreign prices, which outweighed the increase (depreciation) in NEER.

Figure 29: Percentage Contributions to the Change in REER



Source: BSL, staff estimation

3.3.4 Domestic Foreign Exchange Markets

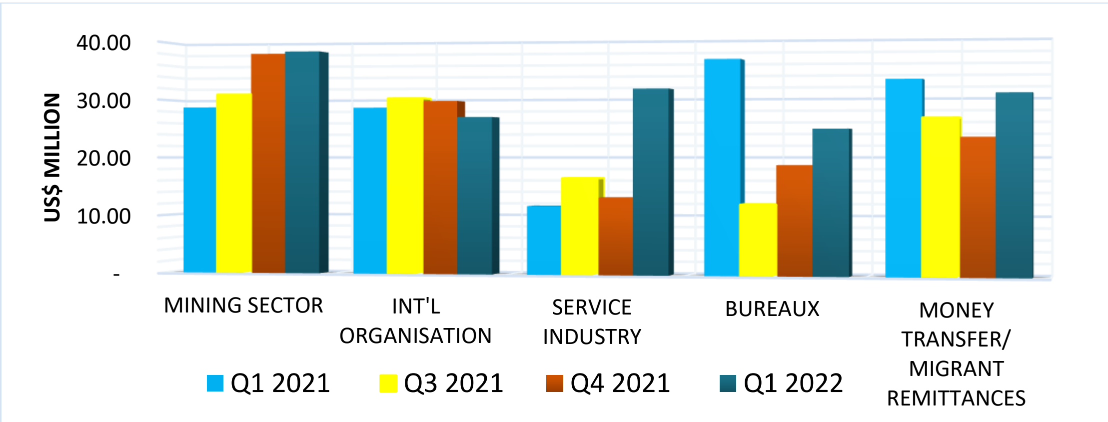
Foreign Exchange Flows

Total amount traded in the foreign exchange market (Purchases and Sales) was US$401.61million in 2022Q1, down by 6.23 percent, relative to US$428.29million recorded in the corresponding quarter (2021Q1) and 16.02 percent above US$346.16million recorded in 2021Q4.

Commercial Banks' Purchases of Forex

Total purchase of foreign exchange by commercial banks increased by 13.62 percent to US$190.06 million in 2022Q1 from US$167.27 million in 2021Q4 on account of increase in purchases made by the mining sector, service industry, bureau, and money transfer agencies/migrant remittances. It decreased by 9.17 percent when compared with US$209.25 million recorded in the corresponding quarter (2021Q1), which could be attributed to the decline in purchases from NGO's/ Int'l organisations, bureaux, and migrant remittances. In May 2022, total purchases was US$93.21million, which is 56.83 percent more than US$59.43 million recorded in April 2022. This was mainly due to funds disbursed under the SFF and RFF, which were direct sales to commercial banks.

Figure 30: Selected Sectors of Purchases of Forex from Commercial Banks



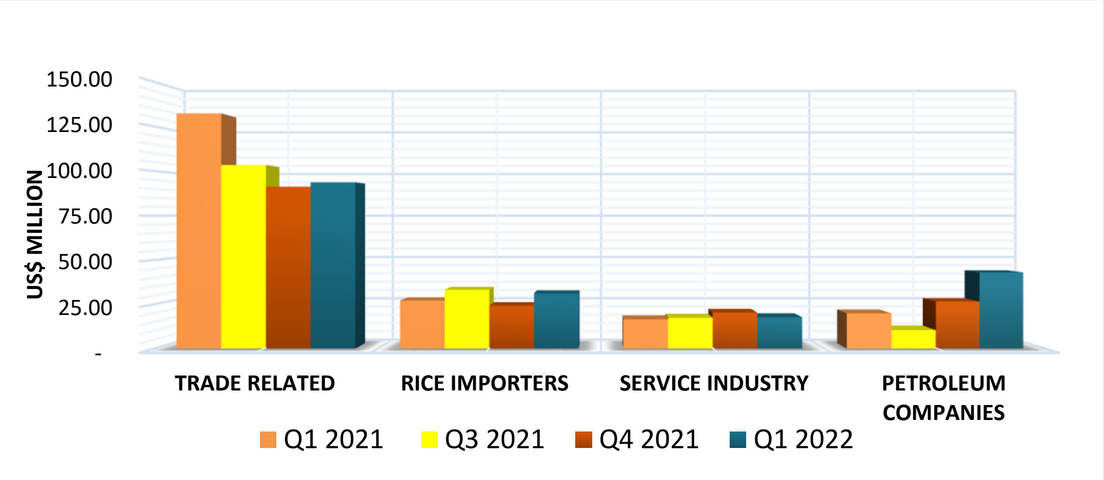
Source: BSL

Commercial Banks' Sales of Forex

Total sales of foreign exchange by commercial banks decreased by 3.42 percent to US$211.55million in 2022Q1, compared to US$219.04million recorded in corresponding period in 2021Q1. The drop in forex sales is mainly attributed to the decline in sales essentially for trade related imports and telecommunication companies. However, it increased by 18.26 percent relative to US$178.89million recorded in 2021Q4 largely due to increase in forex sales for trade related imports, rice importers, petroleum and telecommunication companies. In May

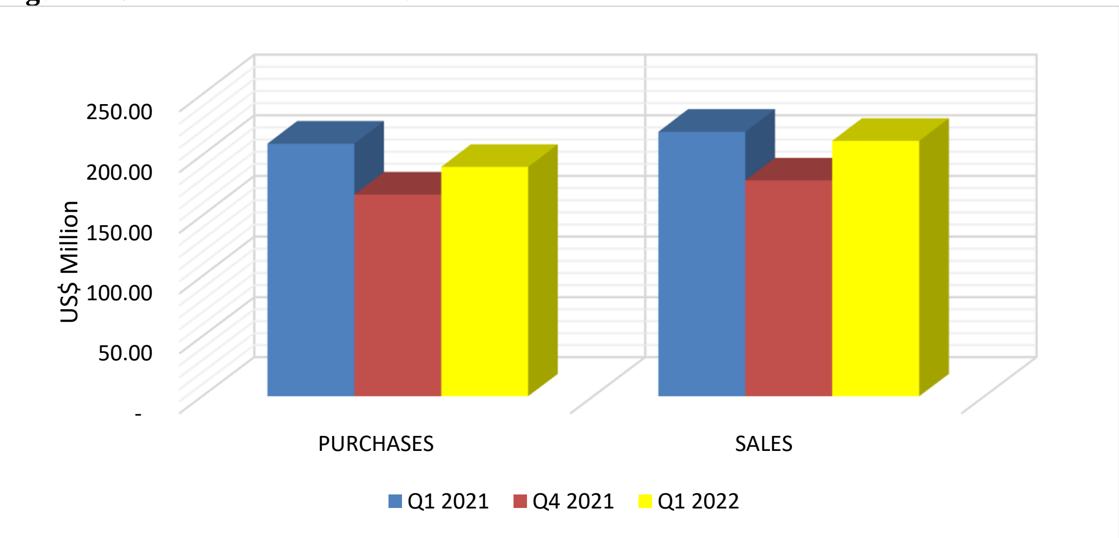
2022, total sales was US$82.42million, 33.97 percent more than the US$61.52million recorded in April 2022.

Figure 31: Selected Sectors of Sales of Forex to Commercial Banks



Source: BSL

Figure 32: Commercial Banks Purchases and Sales of Forex



Source: BSL

3.3.4 Outlook for the Foreign Exchange Market

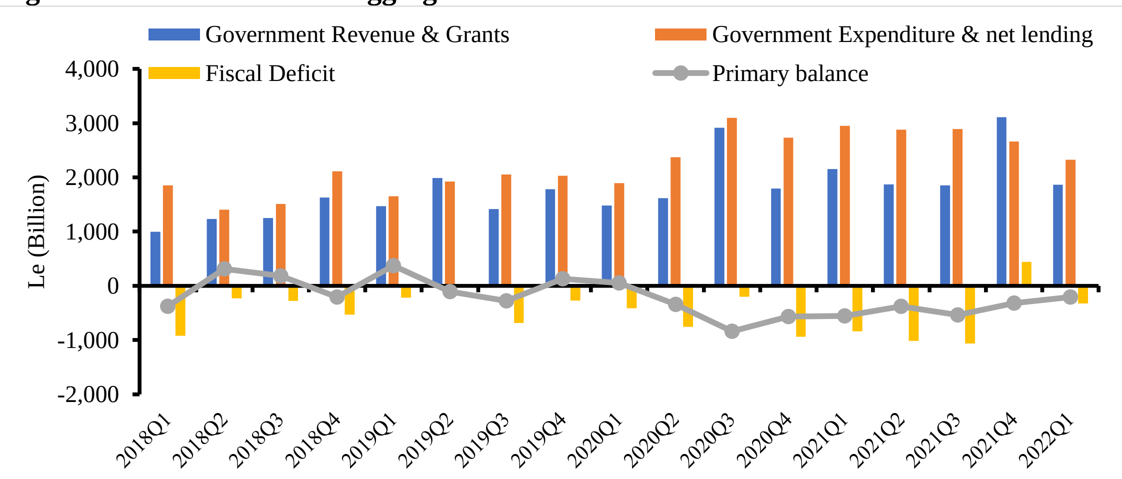
Liquidity constraints in the forex market are expected to persist given the increased demand for foreign exchange for the importation of food and goods associated with the rainy season. Furthermore, the uncertainties in the foreign exchange market is causing some speculative and hedging activities in the FX market, thereby exerting more pressure on the already challenged foreign exchange market. Consequently, the stability of the exchange rates will continue to be challenged given that we are now into the lean period in terms of production and export of minerals, with limited supply of foreign exchange in the market.

3.4 Fiscal Developments

3.4.1 Government Budgetary Operations

Government budgetary operations resulted in an overall deficit of Le324.78 billion in 2022Q1, after recording a surplus of Le439.55 billion in 2021Q4. The deficit ensued from a contraction in total government revenue which more than offset the decline in government expenditure and net lending. Similarly, primary deficit widened to Le204.16 billion in 2022Q1, up from Le32.17 billion in 2021Q4. Figure 2 shows government revenue, expenditure and fiscal deficit and primary balance.

Figure 33: Trends in Fiscal Aggregates



Source: Ministry of Finance

3.4.2 Government Revenues and Grants

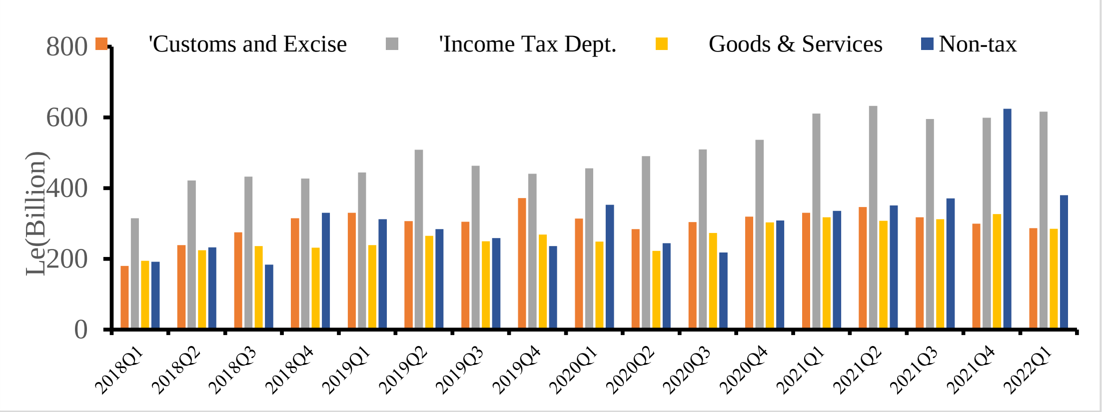
Total revenues and grants contracted by 40.06 percent to Le1, 864.88 billion in 2022Q1 compared to Le3, 111.29 billion in 2021Q4, driven largely by the decrease in foreign grants relative to the dropped in domestic revenue. Foreign grants received declined significantly to Le244.41billion in 2022Q1, down from Le1, 204.79 billion in 2021Q4.

Domestic revenue collected fell to Le1, 620.47 billion in 2022Q1, down from Le1, 906.50 billion in 2021Q4. The contraction in domestic revenue was attributable to the decline in customs & excise, goods & services tax and non-tax revenue, while income tax revenue increased in the review period.

Receipts from goods and services tax fell to Le285.08 billion in 2022Q1 from Le326.99 billion in 2021Q4. Receipt from customs and excise tax dropped slightly to Le286.75billion in 2022Q1 from Le299.77 billion in 2021Q4. Non-tax revenue decreased to Le379.66 billion in 2022Q1 from Le 624.65 billion in 2021Q4. Road user charges declined to Le53.17 billion in 2022Q1 from Le55.86 billion in 2021Q4.

Conversely, revenue generated from income tax increased to Le615.80 billion in 2022Q1 from Le599.23 billion in 2021Q4. **Figure 35** shows components of domestic revenue in 2022Q1 and preceding quarters.

Figure 34: Domestic Revenue Components



Source: Ministry of Finance

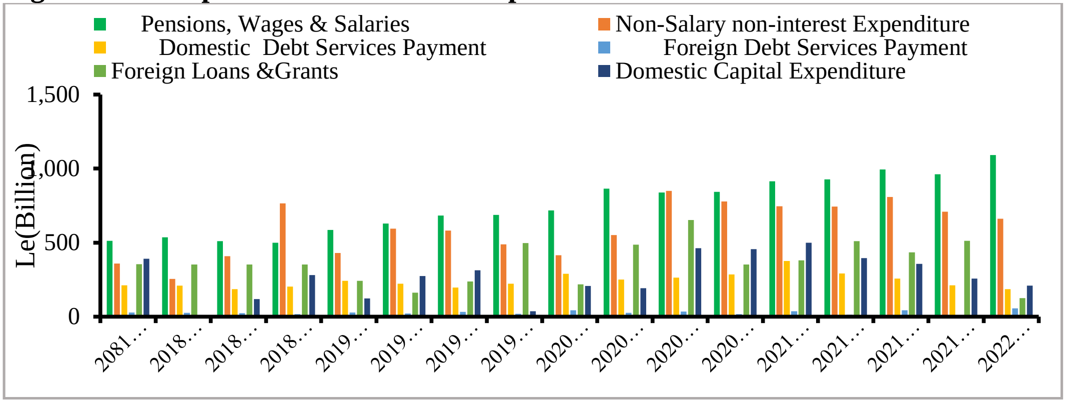
3.4.3 Government Expenditure and Net Lending

Total government expenditure and net lending for the first quarter of 2022 contracted by 12.66 percent to Le2, 324.86 billion, down from Le2, 661.75 billion in 2021Q4. The contraction in government expenditure was due to the decline in capital expenditure, while recurrent expenditure increased in the review quarter.

Recurrent expenditure expanded by 5.19 percent to Le1, 991.86 billion in 2022Q1 from Le 1, 893.57billion in 2021Q4. The expansion in recurrent spending was mainly driven by the increase in total interest payments and the wage bill, yet non-salary non-interest expenditure decreased during the review quarter.

Total interest payments increased to Le240.59 billion from Le221.62 billion in 2021Q4. This amount consists of domestic interest payment amounting to Le184.46billion; and foreign interest payment amounting to Le56.13billion in 2022Q1. Likewise, pension, wages and salaries expanded to Le1,091.14 billion in 2022Q1 from Le962.35 billion in 2021Q4. Non-salary non-interest expenditure, on the other hand declined to Le660.13 billion in 2022Q1 from Le709.61billion in 2021Q4. **Figure 36** shows components of recurrent expenditure in 2022Q1 and preceding quarters.

Figure 35: Components of Recurrent Expenditure



Source: Ministry of Finance

Capital expenditure and net lending contracted by 56.65 percent to Le333.00 billion in the in 2022Q1, down from Le768.18 billion in 2021Q4. This reflects the decrease in both domestic capital expenditure and foreign loans and grants during the review period. Domestic capital expenditure declined to Le208.56 billion in 2022Q1 from Le256.72 billion in 2021Q4. Likewise, foreign loans and grants deceased significantly to Le124.44 billion in 2022Q1 from Le511.46 billion in 2021Q4.

3.4.4 Budget Financing

The overall deficit of Le324.78 billion in 2022Q1 was financed through domestic, foreign and other sources. Of the total deficit, domestic financing amounted to Le767.66 billion, foreign financing amounted to Le70.75 billion, and other sources amounted to Le372.13 billion in 2022Q1.

Domestic financing comprised, bank financing amounting to Le815.89 billion in 2022Q1, while non-bank financing amounted to Le48.23 billion in 2022Q1. The BSL financing increased to Le544.04 billion in 2022Q1 from Le15.20 billion in 2021Q4, while the commercial bank financing reduced to Le271.85 billion in 2022Q1 from Le279.83 billion in 2021Q4.

3.4.5 Outlook for the Fiscal Sector

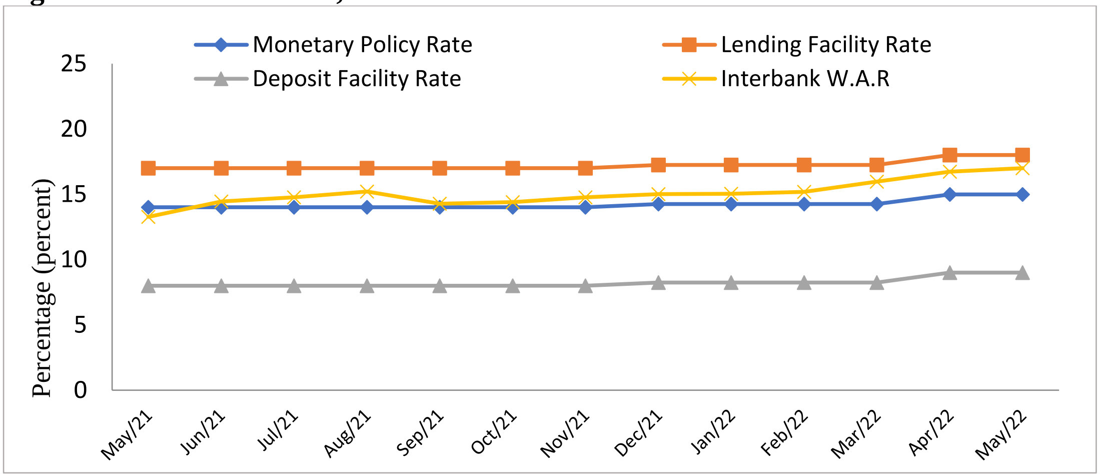
Fiscal operations are expected to remain challenged at least in the near term given the high expenditure requirements of the government to support the recovery program and financing of the general elections in 2023. However, expected improvement from domestic revenue with the commencement of iron ore operations, and coupled with expected inflows from development partners may help to moderate the likely fiscal pressures.

3.5 Monetary Policy, Money and Financial Markets Developments

3.5.1 Monetary Policy Stance

The Monetary Policy Committee (MPC) met in March 2022 and decided to raise the Monetary Policy Rate (MPR) by 75 basis points from 14.25 percent to 15.0 percent. Similarly, the Policy corridor - the Standing Lending Facility rate and the Standing Deposit Facility rate were increased by the same margin to 18.0 percent and 9.0 percent in March 2022, respectively. The decision of the MPC was informed by its assessment of developments in the international and domestic economy and their implication for inflation outlook.

Figure 36: Trends in MPR, Interbank and Corridor Rates

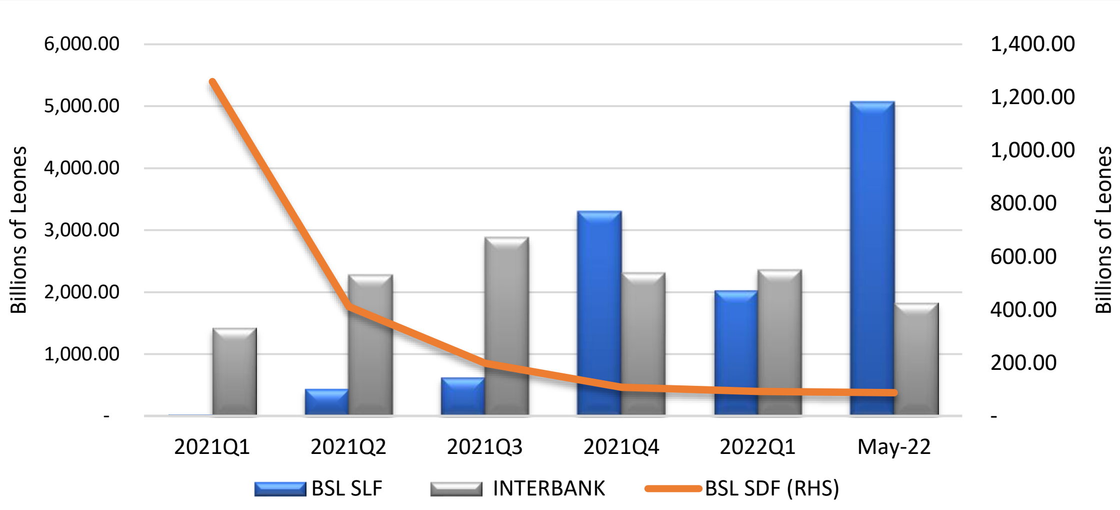


Source: BSL

3.5.2 Interbank Money Market Rate

The level of intermediation in the interbank money market increased during the review period, with the volume of interbank transactions increasing by 1.90 percent to Le2,358.50 billion in 2022Q1, and stood at Le1,825.20 billion at end May, 2022. Access to the BSL Standing Deposit Facility (SDF) window decreased by 13.62 percent to Le93.20 billion in 2022Q1 and stool at Le88.20 billion at end May 2022. Also, access to the BSL Standing Lending Facility (SLF) window decreased by 150.00 percent to Le2,031.00 billion in 2022Q1, and stood at Le5,071.50 billion at end May, 2022.

Figure 37: Volume of Transactions in the Interbank Market and BSL Standing Facility Windows



Source: BSL

3.5.3 Developments in Monetary Aggregates

Developments in the monetary aggregates were mixed during the first quarter of 2022, as Broad Money (M2) expanded whilst Reserve Money (RM) contracted.

Broad Money (M2)

Broad Money (M2) growth moderated to 5.36 percent in 2022Q1, relative to 10.73 percent in 2021Q4. The slowdown in M2 growth mainly reflected the deterioration in Net Foreign Assets (NFA) of the banking system, which somewhat dampened the growth in the Net Domestic Assets (NDA) of the banking system.

Growth in NFA of the banking system reduced to 2.53 percent in 2022Q1, compared to the 30.13 percent expansion in 2021Q4. The moderation in the growth in NFA of the banking system was on account of the deterioration in the NFA of the Bank of Sierra Leone albeit the NFA of the commercial banks expanded by 15.97 percent.

NDA of the banking system expanded by 6.27 percent in 2022Q1, following a growth of 5.70 percent in 2021Q4. This development was mainly driven by the growth in net claims on Government by both the Bank of Sierra Leone and the commercial banks. Net claims on Government by the BSL grew by 6.59 percent in 2022Q1, relative to the 0.17 percent increase in 2021Q4. Net claims on Government by commercial banks expanded by 11.59 percent in 2022Q1 following a contraction of 1.50 percent in 2021Q4, mainly due to increase in their holdings of Government securities.

In terms of annual growth rate, M2 expanded by 23.49 percent in 2022Q1 compared to the 22.05 percent increase in 2021Q4, and relative to the IMF/ ECF program target of 9.70 percent for 2022Q1.

From the liability side, Narrow Money (M1) grew by 1.15 percent in 2022Q1 from 14.01 percent increase in 2021Q4, due to the 5.80 percent increase in demand deposits which more than offset the 4.28 percent contraction in currency outside banks. Quasi Money (RM) expanded by 10.01 percent in 2022Q1, compared to the 7.34 percent increase in 2021Q4 as a result of expansion in both foreign currency deposits (15.36 percent) and time and savings deposits (3.64 percent).

Reserve Money (RM)

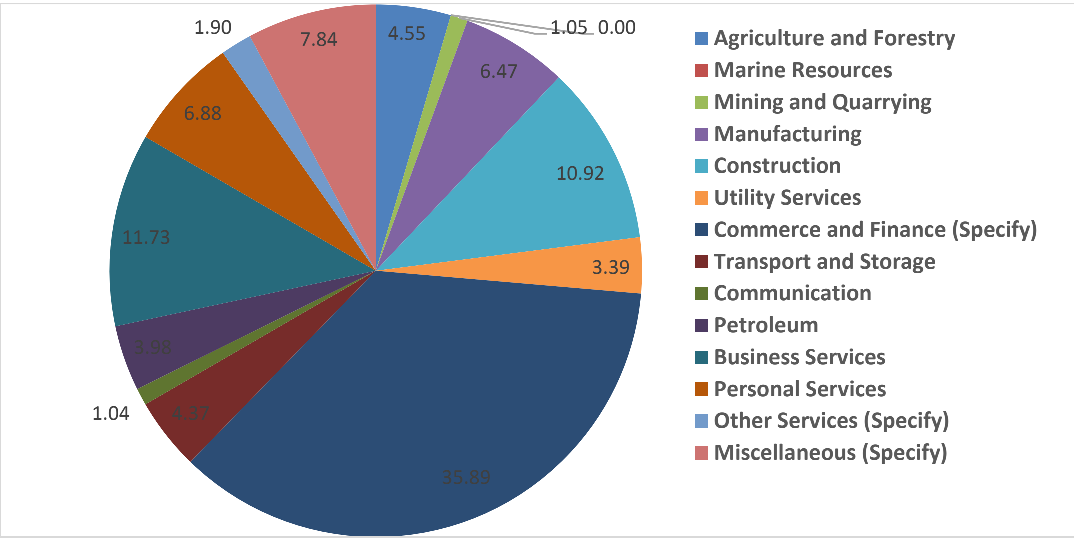
RM contracted by 2.15 percent in 2022Q1, from an expansion of 14.47 percent in 2021Q4 (Table 4). The contraction in RM was on account of deterioration in Net Foreign Assets (NFA) of the BSL, which was more than the expansion in Net Domestic Assets (NDA) of the BSL. NFA of the BSL deteriorated in 2022Q1 reflecting a drawdown in foreign reserves for the settlement of official foreign transactions. NDA of the BSL expanded by 8.30 percent in 2022Q1, from 9.76 percent increase in 2021Q4. The expansion in NDA was mainly due to increase in net claims on Government by the BSL. On annual basis, RM grew by 8.74 percent in 2022Q1, compared to 8.68 percent in 2021Q4, and the IMF/ECF program target of 4.9 percent for 2022Q1.

From the liabilities side, both currency issued and banks' reserves contracted by 2.49 percent and 0.74 percent, respectively, which translated into a contraction in RM in 2022Q1.

Private Sector Credit

Credit to the private sector by the commercial banks increased by 1.59 percent in 2022Q1, compared to the 8.27 percent growth in 2021Q4, and the IMF/ ECF program target of 14.40 percent in 2022Q1. The moderation in private sector credit reflects reduced economic activity during the review period. On a year-on-year basis, growth in Private Sector credit slowed down to 24.83 percent in 2022Q1 relative to the 33.89 percent in 2021Q4.

Figure 38: Dynamics of Sectorial Share of Gross Loans and NPLs



Source: BSL

The Commerce and Finance, Business Services and the Construction sectors dominated the loan portfolios of the banking sector in the first quarter of 2022. These three sectors accounted for 58.54 percent of gross loans in 2022Q1. Also, they accounted for 69.64 percent of the NPLs in the banking sector with each contributing 38.04 percent, 13.44 percent and 23.40 percent respectively to total NPLs. However, the sector with the largest NPL was the Construction sector, followed by the Other services sector and Mining and Quarrying Sector with an NPL of 31.49 percent, 28.93 percent and 26.21 percent respectively.

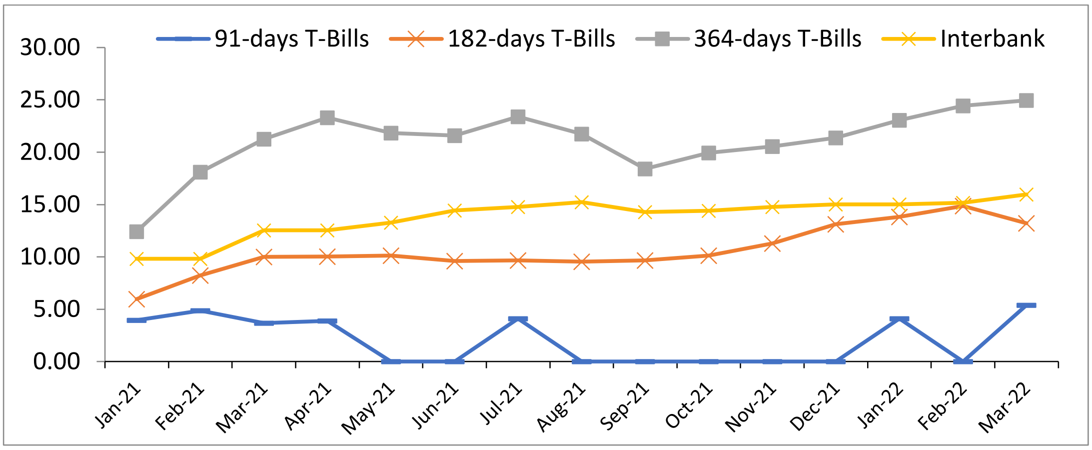
3.5.4 Interest Rates Developments

Treasury Bills and Interbank Rates

During the review period, the annual yield on the 364-day Treasury Bills increased by 357 basis points to 24.95 percent in March, 2022, and further increased to 25.04 percent in May, 2022. The annual yield on the182-day Treasury bills remained unchanged at 13.21percent in May, 2022. The annual yield on the 91-day Treasury bills increased by 129 basis points to 5.40 percent in March, 2022. There was also no demand for 91-days tenure in May, 2022.

The interbank weighted average yield increased from 15.01percent in December, 2021 to 15.96 percent in March, 2022, and further to 17.00 percent in May, 2022. The increase could be attributed to the emergence of liquidity pressure in the banking system. **Figure 40** shows the trends in yields of Government securities in both the Primary and Interbank markets for the period May, 2021 to May 2022.

Figure 39: Trends in the Yields of Government Securities

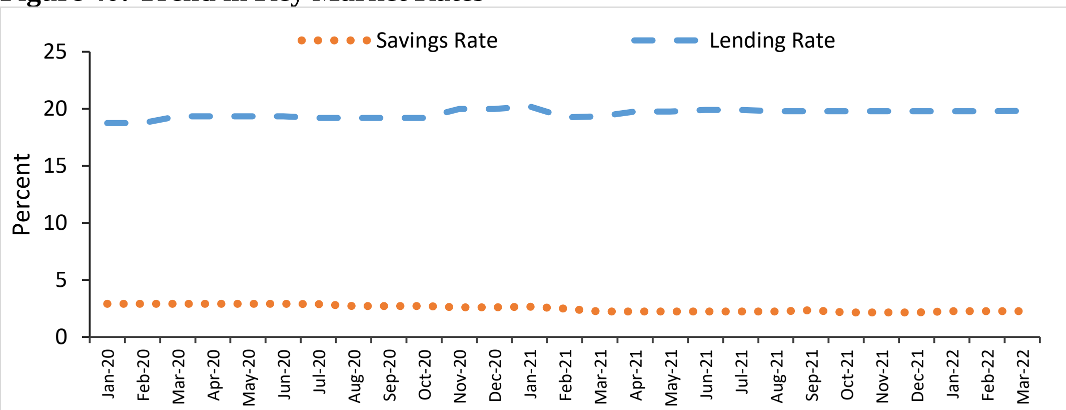


Source: BSL

Commercial Banks' Rates

The average lending rate of commercial banks increased slightly from 19.77 percent in December 2021 to 19.81 percent in March 2022. Similarly, the saving deposits rate increased marginally from 2.15 percent in December 2021 to 2.27 percent in March 2022. However, the spread between commercial banks' lending rate and saving rate remains high.

Figure 40: Trend in Key Market Rates



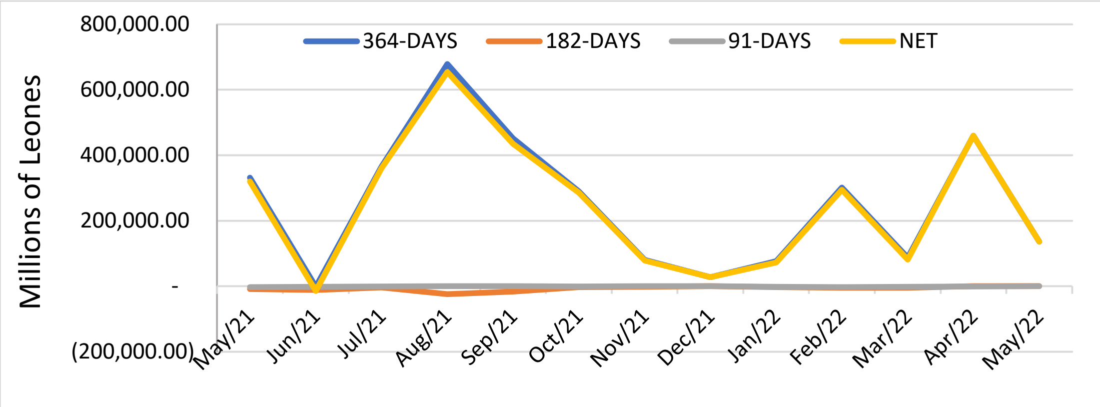
Source: BSL

3.6 Domestic Debt Developments

3.6.1 Primary Market Auction Outcomes

The primary market for Government securities were mostly oversubscribed on net basis in the review period, driven largely by the 364-day Treasury bills. The 364-days tenure was largely oversubscribed, whilst the 182-days and the 91-days tenures were undersubscribed in 2022Q1, and continued in May, 2022. There was no transactions for 91-days tenure in May 2022.

Figure 41: Under/Oversubscription of T-Bills Auctions in the Primary Market



Source: BSL

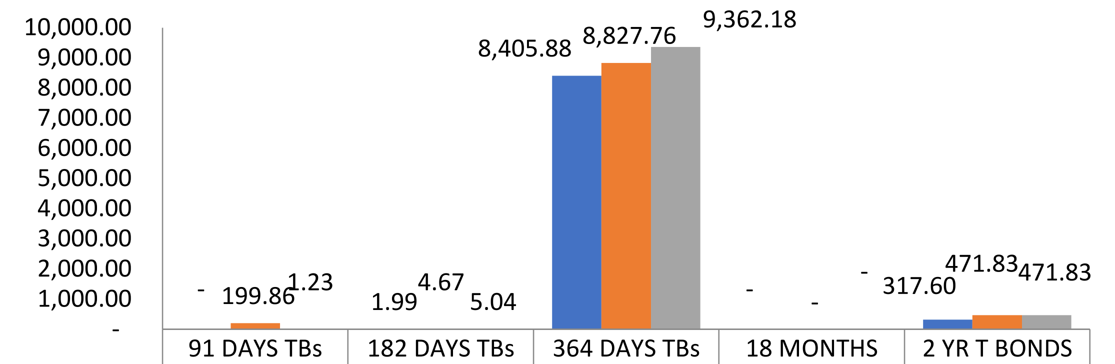
3.6.2 Stock of Government Securities

The total stock of Government securities increased 9.07 percent from Le9,458.14 billion as at end December, 2021 to Le10,315.65 billion as at end March, 2022, and further to Le10,925.24 billion as at end-May, 2022. Marketable securities accounted for 92.13 percent of the total stock of Government securities in March 2022 and 90.07 percent in May 2022, whilst non-marketable securities accounted for 7.87 percent in March 2022 and 9.93 percent May, 2022.

The stock of marketable securities increased by 8.92 percent to Le9,504.11billion as at end-March, 2022, and further to Le9,320.86 billion as at end-May, 2022. The stock of non-marketable securities increased by 10.76 percent to Le811.53 billion as at end-March, 2022, and further to Le1,084.96 billion as at end-May, 2022.

the proportion of 91-day Treasury bills, 182-day Treasury bills and 364-day Treasury bills to total marketable securities were 2.10 percent, 0.05 percent and 92.88 percent respectively at end March, 2022. The 2-year Treasury bonds accounted for 4.96 percent. With regards non-marketable securities, the 3-year Treasury bond, 5-year Treasury bond and 10-year Treasury bond accounted for 64.70 percent, 33.92 percent and 1.38 percent respectively.

Figure 42: Stock of Marketable Government Securities by Tenure



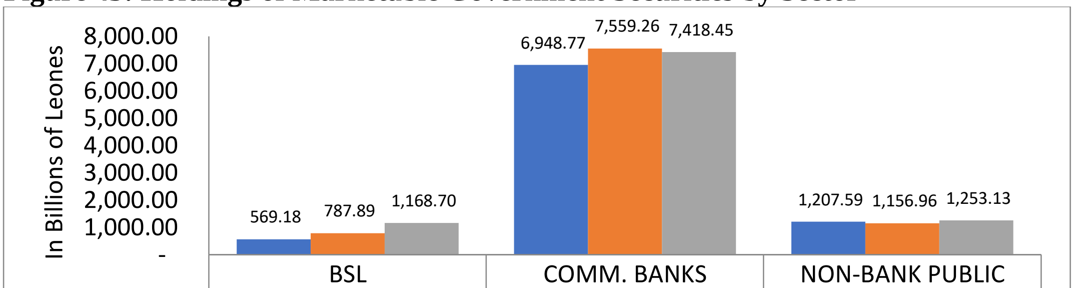
	91 DAYS TBs	182 DAYS TBs	364 DAYS TBs	18 MONTHS	2 YR T BONDS
Dec-21	-	1.99	8,405.88	-	317.60
Mar-22	199.86	4.67	8,827.76	-	471.83
May-22	1.23	5.04	9,362.18	-	471.83

Source: BSL

3.6.3 Distribution of the Stock of Government Securities by Sector

The holdings of marketable Government securities increased for all the sectors during the review period. The holdings of marketable Government securities by the commercial banks increased from Le6,948.77 billion as at end-December, 2021 to Le7,559.26 billion as at end-March, 2022, but decreased to Le7,418.45 billion as at end-May, 2022. Non-bank holdings of marketable Government securities declined from Le1, 207.59 billion as at end December 2021 to Le1,156.96 billion as at end-March 2022, but increased to Le1,253.13 billion as at end-May 2022. BSL holdings of marketable Government securities increased from Le569.12 billion as at end-December, 2021 to Le787.89 billion as at end-March, 2022, and further to Le1,168.70 billion as at end-May, 2022.

Figure 43: Holdings of Marketable Government Securities by Sector



	BSL	COMM. BANKS	NON-BANK PUBLIC
Dec-21	569.18	6,948.77	1,207.59
Mar-22	787.89	7,559.26	1,156.96
May-22	1,168.70	7,418.45	1,253.13

Source: BSL

3.7 Financial Stability Analysis

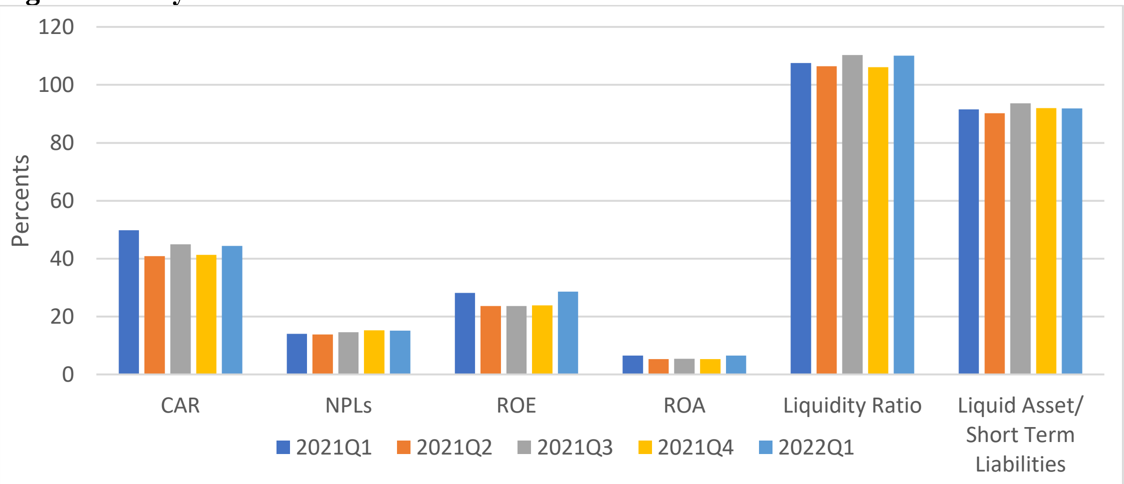
The Banking sector continued to be relatively stable, liquid and profitable during the review period. Almost all the key Financial Soundness Indicators (FSIs) were above their minimum regulatory limits, expect for Non-performing Loans (NPLs) ratio, which although declined marginally remained above the minimum threshold in 2022Q1. Government securities remain the largest asset of banks, and therefore the main source of income for banks. Gross loans decreased marginally in 2022Q1, while Treasury bills holdings increased financed by increased deposits of the banking sector.

3.7.1 Financial Soundness Indicators (FSIs)

The banking sector continued to be relatively stable- liquid, profitable and capitalised. The key FSIs were above their thresholds stipulated by BSL except for the Non-performing Loan (NPLs) ratio, which remain above the minimum threshold. The regulatory capital to risk-weighted asset increased to 44.45 percent in 2022Q1 from 41.31 percent in 2021Q4, mainly due to the increase in revaluation reserves, issued and paid up capital and retained earnings.

Asset quality improved slightly with the ratio of Non-performing Loans to total loans decreasing marginally to 15.13 percent in 2022Q1 from 15.23 percent in 2021Q4. Return on asset (ROA) and return on equity (ROE) were 6.52 percent and 28.62 percent respectively for 2022Q1, compared to 5.36 percent and 23.86 percent respectively in 2021Q4. The liquidity in the Banking Sector slightly improved during the review period, as Liquidity Ratio increased to 110.05 percent in 2022Q1 from 106.14 percent in 2021Q4. **Figure 45** below shows the key FSIs of the banking sector.

Figure 44: Key FSI's Indicators



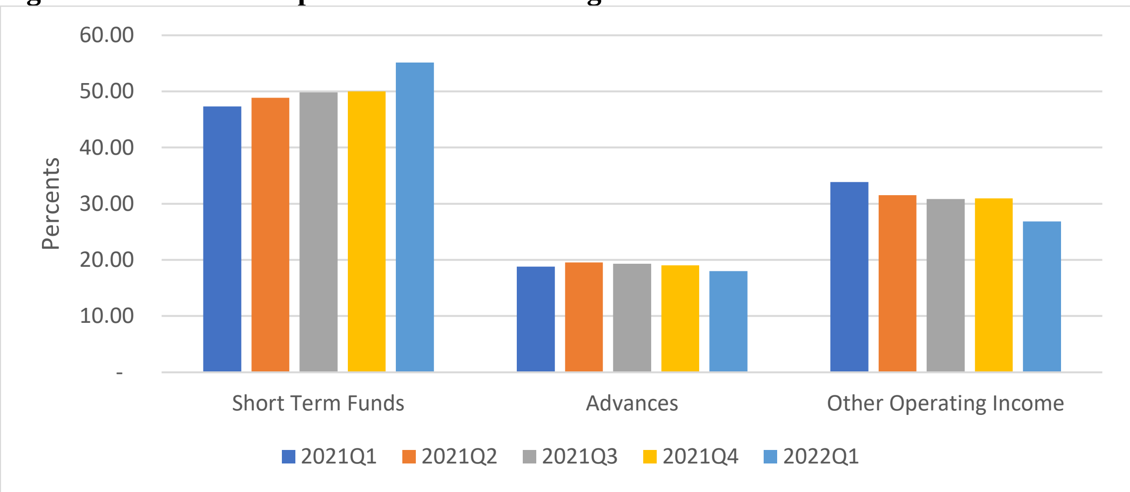
Source: BSL

3.7.2 Income Composition

The banking sector continued to rely primarily on government securities for its income. This is mainly due to relatively high yields on Government securities with nil risk of investments. In 2022Q1, the proportion of income from short term funds increased by 5.59 percent but income from advances decreased 19.03 percent as at end 2021Q4 to 17.99 percent as at end 2022Q1. The increase in income from short term funds may be attributed to the increase in the one year Treasury bills rate to 24.95 percent in 2022Q1 from 21.38 percent in 2021Q4.

However the proportion of Other Operating income declined from 30.95 percent in 2021Q4 to 26.85 percent in 2022Q1. Other operating income comprised mainly commission, fees and profit on foreign exchange dealings. **Figure 46** below shows the composition of income in the banking sector.

Figure 45: Income Composition for the Banking Sector

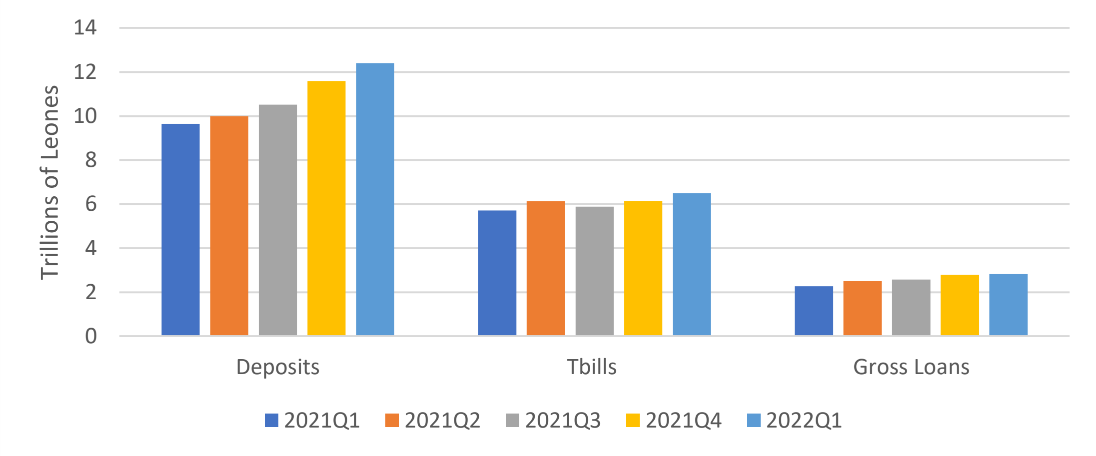


Source: BSL

3.7.4 Sources and Utilization of Funds

Total deposits, the main source of funds for banks, increased by 7.08 percent in 2022Q1 from Le 11.59 trillion in 2021Q4 to Le12.41 trillion in 2022Q1. Treasury bills holding by the banking sector increased by 5.53 percent from Le6.15 trillion in 2021Q4 to Le6.49 trillion in 2022Q1. Gross loans and advances also increased by 1.43 percent from Le2.79 trillion in 2021Q4 to Le2.83 trillion in 2022Q1.

Figure 46: Trend in Deposits, Treasury Bills and Gross Loans

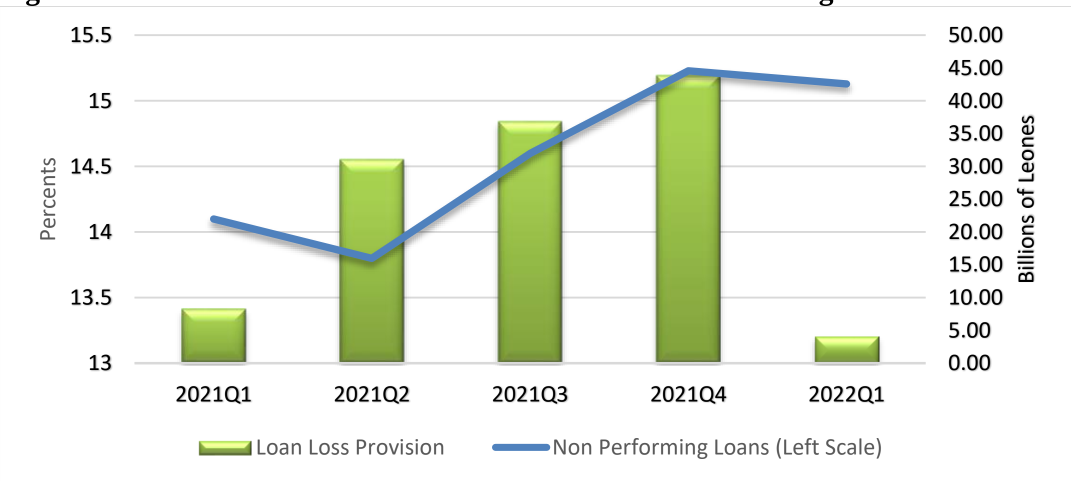


Source: BSL

3.7.5 Trends in NPL and Loan Loss Provisions

After increasing during the previous three quarters, the NPLs ratio declined from 15.23 percent in 2021Q4 to 15.13 percent in 2022Q1. Accordingly, Loan loss provision was less than the amount of provision in the same period due to the decrease in NPLs. Loan loss provision in 2022Q1 declined to Le4.08 billion in 2022Q1, relative to LeLe43.90 billion in 2021Q4. **Figure 48** below shows the trend of NPLs and Loan Loss provision in the banking sector.

Figure 47: Trend in NPLs and Loan Loss Provision in the Banking Sector



Source: BSL

3.7.6 Challenges

The War in Ukraine continued to pose major risks to the economy of Sierra Leone and by implication the stability of the banking sector. The surge in commodity, food and energy prices brought about by the Russia-Ukraine crises and the disruptions of global supply chains are downside risks to the economy. Global financial market volatility and the threat of recession in the western world have far reaching implication on the stability and resilience of the banking sector. The spillover effect of sanctions brought about as a result of the war are expected to have negative effect on most Emerging Markets and Developing Economies. Delays in the payment of government arrears may also deteriorate the quality of asset portfolio of selected banks. The volatility in the foreign exchange market also poses a challenge to the banking sector.

3.7.7 Outlook

The banking sector will continue to be relatively stable in the immediate future. However the War in Ukraine continue to create uncertainties leading to spiraling food and energy prices which has the potential to disrupt economies and by implication the financial system. Nonetheless, increased government borrowing will continue to provide risk free investment opportunities for banks thereby improving the risk weighted assets of the banking sector. Interest from investment in government securities will continue to be the main source of income for banks. And banks will be better placed to withstand future challenges with the improvement in the CAR. However, rising prices in the construction sector may disrupt construction contracts increasing the risk of increased NPL in the banking sector.

4. CONCLUSION AND DECISION OF THE MONETARY POLICY COMMITTEE

4.1 CONCLUSION

Domestic economic activities recovered by more than expected in 2021, with real GDP growth revised upward to 3.2 percent in 2021, compared to the initial projection of 2.9 percent. The development largely reflected higher than expected performance in all the growth enhancing sectors of the economy, including mining and agriculture sectors.

Nevertheless, the growth prospects for 2022 have been revised downwards, with real GDP growth downgraded to 3.6 percent for 2022 from an earlier estimate of 6.0 percent. The revision largely reflects the effects of Russia's war on Ukraine and the induced rising energy and food prices, global supply disruptions, and the lingering effects of the COVID-19 pandemic. Risks associated with the attainment of the 3.6-percent-growth forecast are tilted to the downside, and may largely depend on the duration of the Russia-Ukraine war and the extent of its spillovers to small open economies like Sierra Leone.

Domestic inflationary pressures remains elevated, driven mainly by the effects of the COVID-19 pandemic, the Russia-Ukraine War, and the associated sanctions imposed on Russia, all of which have produced significant increases in commodity prices (particularly food and energy prices), disruptions in the global supply chain and increased freight charges. In addition, the restrictive monetary policies implemented by advanced economies have led to the tightening of financial conditions and exchange rate pressures in small-open economies like Sierra Leone.

These developments have caused a sharp increase in headline inflation, which increased from 17.94 percent in the fourth quarter of 2021 to 22.06 percent in the first quarter of 2022, and further to 24.87 percent in May 2022.

However, it must be noted that the current inflationary pressures are global in nature and not unique to Sierra Leone. The current price increases are largely driven by supply-side factors, for which demand-side instruments (such as monetary policy tools) are by themselves inadequate—especially in an environment of stagflation. Hence, tight monetary policy stance, needs to be supported by fiscal policy reforms that would boost total factor productivity particularly in the agricultural sector.

4.2 DECISION OF THE MONETARY POLICY COMMITTEE

The Monetary Policy Committee noted that inflationary pressures have persisted, and that it is expected to remain on an elevated path in the next few quarters, due mainly to supply-side factors including, rising global commodity prices, higher freight charges, disruption in global supply chain, uncertainty surrounding the COVID-19 pandemic and the Russian-Ukrainian war. The MPC also noted with concern the persistent increase in domestic prices and the likely effects on the welfare of the people, particularly the poor. Because of the environment of stagflation in which the economy is currently anchored, the MPC recommended supply-side policy reforms to increase aggregate supply, thereby concurrently lowering the price level and boosting economic growth. Mindful of the BSL's responsibility for safeguarding price and financial-system stability, while supporting economic growth, the MPC decided to raise the Monetary Policy Rate (MPR) by 100 basis points to 16.0 percent as a short-term anti-inflationary measure. The MPC also adjusted the Standing Lending Facility Rate and the Standing Deposit Facility rate upward to 19.0 percent and 10.0 percent respectively.

The MPC will continue to monitor developments in the global and domestic macroeconomic and financial environment and stands ready to take appropriate actions should they adversely impact price and financial-system stability.

Appendix

Table 1: Global and Regional GDP Growth Rates

		Estimates	WEO Jan. 2022 Updates		WEO April 2021 Proj.		CHANGE IN Projections	
	2020	2021	2022	2023	2022	2023	2022	2023
World Output	**-3.1**	**6.1**	**4.4**	**3.8**	**3.6**	**3.6**	**-0.8**	**-0.2**
Advanced Economies	-4.5	5.2	3.9	2.6	3.3	2.4	-0.6	-0.2
United States	-3.4	5.7	4.0	2.6	3.7	2.3	-0.3	-0.3
Euro Area	-6.4	5.3	3.9	2.5	2.8	2.3	-1.1	-0.2
United Kingdom	-9.3	7.4	4.7	2.3	3.7	1.2	-1.0	-1.1
Japan	-4.5	1.6	3.3	1.8	2.4	2.3	-0.9	0.5
Emerging Market and Developing Economies	**-2.0**	**6.8**	**4.8**	**4.7**	**3.8**	**4.4**	**-1.0**	**-0.3**
Brazil	-3.9	4.6	0.3	1.6	0.8	1.4	0.5	-0.2
Russia	-2.7	4.7	2.8	2.1	-8.5	-2.3	-11.3	-4.4
India	-6.6	8.9	9.0	7.1	8.2	6.9	-0.8	-0.2
China	2.2	8.1	4.8	5.2	4.4	5.1	-0.4	-0.1
Sub-Saharan Africa	**-1.7**	**4.5**	**3.7**	**4.0**	**3.8**	**4.0**	**0.1**	**0.0**
Nigeria	-1.8	3.6	2.7	2.7	3.4	3.1	0.7	0.4
South Africa	-6.4	4.9	1.9	1.4	1.9	1.4	0.0	0.0
Angola	-5.6	0.7	2.9	3.3	3.0	3.3	0.1	0.0

Table 2: Monetary Policy Stance of Selected Central Banks

Country	Monetary Policy Rate		Change in Policy rate	Projection
	Previous	Current		
USA	0.5	1	0.5	1.5
Euro Area	0.00	0.00	0	0.00
China	3.70	3.70	0	3.70
Nigeria	11.50	13.00	1.5	11.50
Ghana	17.00	19.00	2	19.00
Guinea	11.50	11.50	0	11.50
Liberia	20.00	20.00	0	20.00
The Gambia	10.00	10.00	0	12.00

Primary Source: Central Banks March-May 2022, collected from Trading Economics June, 2022

Table 3: Money Supply and its Components

	2021	2022	Quarterly percent change		Yearly percent change	
Billions of Leones	**Q4**	**Q1**	**2021Q4**	**2022Q1**	**2021Q4**	**2022Q1**
Reserve money	**4,602.18**	**4,503.28**	**14.47**	**(2.15)**	**8.68**	**8.74**
Broad money (M2)	**14,391.06**	**15,163.12**	**10.73**	**5.36**	**22.05**	**23.49**
Narrow money (M1)	**7,539.77**	**7,626.27**	**14.01**	**1.15**	**25.58**	**22.52**
Currency outside banks	3,479.76	3,330.65	18.45	(4.28)	23.97	11.50
Demand deposit	4,060.01	4,295.61	10.45	5.80	27.00	32.68
Quasi Money	**6,851.29**	**7,536.85**	**7.34**	**10.01**	**18.39**	**24.49**

o.w. Foreign currency deposit	3,703.87	4,272.91	14.01	15.36	32.39	43.33
Time and saving deposit	3,142.45	3,256.90	0.43	3.64	5.92	6.22
Net Foreign Asset	**3,482.71**	**3,570.92**	**30.13**	**2.53**	**8.67**	**17.42**
BSL	(169.31)	(664.21)	(48.23)	292.29	(127.17)	(434.10)
ODCs	3,652.03	4,235.12	21.60	15.97	41.46	49.01
Net Domestic Assets	**10,908.35**	**11,592.20**	**5.70**	**6.27**	**27.05**	**25.49**
Net Domestic Credit	**13,260.34**	**14,268.79**	**0.28**	**7.61**	**21.73**	**21.68**
Government (Net)	**10,387.50**	**11,371.44**	**(0.79)**	**9.47**	**19.63**	**22.04**
o.w.BSL	4,407.14	4,697.75	0.17	6.59	23.88	18.78
ODCs	5,980.36	6,673.69	(1.50)	11.59	16.68	24.44
Private Sector	**3,161.95**	**3,213.36**	**8.20**	**1.63**	**32.86**	**24.68**
o.w. ODCs	3,145.16	3,195.24	8.27	1.59	33.89	24.83
Other Sectors (Net)*	(289.11)	(316.01)	70.91	**9.31**	70.00	**87.36**
Other Items (Net)	**(2,351.99)**	**(2,676.59)**	**(19.01)**	**13.80**	**1.97**	**7.54**
Money Multiplier	3.13	3.37				

Table 4: Reserve Money and Components

	2021	2022	Quarterly percent Change		Yearly percent Change	
Billions of Leones	**Q4**	**Q1**	**2021Q4**	**2022Q1**	**2021Q4**	**2022Q1**
Net Foreign Assets	**(169.31)**	**(664.21)**	**(48.23)**	**292.29**	**(127.17)**	**(434.10)**
Net Domestic Assets	**4,771.50**	**5,167.48**	**9.76**	**8.30**	**32.12**	**31.07**
Government Borrowing (net)	**4,407.14**	**4,697.75**	**0.17**	**6.59**	**23.88**	**18.78**
o.w. 2.11 Securities	1,110.22	1,256.00	4.24	13.13	9.77	7.79
2.12 Ways and Means	196.19	244.38	11.10	24.56	(8.14)	158.25
2.13 GoSL/IMF Budget financing	3,365.50	3,257.33	(0.69)	(3.21)	33.28	7.40
Reserve money	**4,602.18**	**4,503.28**	**14.47**	**(2.15)**	**8.68**	**8.74**
o.w. 3.1 Currency issued	3,827.19	3,731.93	17.70	(2.49)	27.19	16.01
3.2 Bank reserves	770.04	764.30	0.78	(0.74)	(35.99)	(16.70)

Source: Research Dept. Bank of Sierra Leone

Table 5: Interest Rates

	2021										**2022**		
	Mar	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**
91-day T-Bills		3.90	0.00	0.00	4.11	0	0	0	0	0	4.11	0	5.40
182-day T-Bills	10	10.03	10.13	9.61	9.67	9.54	9.67	10.14	11.3	13.13	13.82	14.85	13.21
364-day T-Bills	21.25	23.31	21.83	21.59	23.39	21.75	18.4	19.94	20.56	21.38	23.07	24.43	24.95
Interbank rate	12.53	12.53	13.28	14.45	14.77	15.22	14.29	14.41	14.77	15.01	15.03	15.18	15.96
SLF	17.00	17.00	17.00	17.00	17.00	17.00	17.00	17.00	17.00	17.25	17.25	17.25	17.25
SDF	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.25	8.25	8.25	8.25
MPR	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.25	14.25	14.25	14.25
Av. Lending rate	19.33	19.74	19.74	19.88	19.88	19.88	19.77	19.77	19.77	19.77	19.77	19.77	19.81
Lending (Prime)	18.02-20.64	18.83-20.64	18.83-20.64	19.11-20.64	19.11-20.64	19.11-20.64	19.03-20.50	19.03-20.50	19.03-20.50	19.03-20.50	19.03-20.51	19.03-20.51	19.11-20.50
Savings deposits	2.23	2.23	2.23	2.23	2.23	2.23	2.36	2.15	2.15	2.15	2.27	2.27	2.27

Table 6: Forecast Outcomes for ARIMA and ARIMAX

Quarterly Outlook	ARIMAX	ARIMA	BVAR Forecast
2022Q2 (M06)	25.13percent	25.8percent	26.97percent
2022Q3 (M09)	23.66percent	27.8percent	27.39percent

Source: Staff Computation

Table 7: Contribution for all items in the CPI basket

	Mar-22	Apr-22	May-22	Jun-22*	Jul-22*	Aug-22*	Sep-22*	Oct-22*	Nov-22*	Dec-2
Headline Consumer Price Index	**22.1**	**22.4**	**24.9**	**25.8**	**27.2**	**27.9**	**27.8**	**28.3**	**28.7**	27
Communication	9.6	10.2	9.6	8.1	3.9	5.1	-0.3	0.9	0.6	-4
Transportion	33.9	35.3	35.0	30.5	34.2	30.7	31.6	38.0	42.8	42
Furnishing and household equipment	27.4	30.8	32.6	34.8	31.9	31.3	27.1	29.4	27.7	23
Clothing , textile and footwear	8.1	6.8	11.4	11.7	11.5	13.0	12.9	13.3	13.7	11
Housing, fuel and lightening	17.8	18.1	18.9	18.7	21.2	20.2	20.4	20.6	21.7	19
Food and drink	22.8	22.9	26.7	27.6	30.0	32.2	34.9	34.8	35.5	34
Health	18.5	17.1	19.0	22.9	20.9	22.2	20.9	19.0	20.0	16
Miscelaneous	13.5	16.8	19.0	21.9	21.1	19.8	18.9	18.7	16.3	16
Recreation and culture	30.9	31.8	35.1	35.4	36.4	35.7	33.1	30.9	26.5	20
Hotels, cafe and restaurants	34.0	35.9	36.3	41.2	45.2	48.5	46.5	50.4	49.0	48
Alcohol, beverages and tobaco	21.7	17.3	19.1	21.1	19.0	15.8	13.3	15.5	15.9	16
Education	37.5	37.4	37.8	40.0	42.5	37.1	16.1	5.8	3.9	3

Table 8: Stock of Government Securities Outstanding by Tenure and by Holder

STOCK OF GOVERNMENT SECURITIES OUTSTANDING BY TENOR AND BY HOLDER (IN MILLIONS OF LEONES)					
	Dec-21	Mar-22	May-22	Change (Dec 21-Mar 22)	Change (Mar 22-May 22)
91 DAYS TBs	**-**	**199,859.15**	**1,233.90**	**199,859.15**	**(198,625.25)**
BSL	-	198,175.25	-	198,175.25	(198,175.25)
COMM. BANKS	-	-	-	-	-
NON-BANK PUBLIC	-	1,683.90	1,233.90	1,683.90	(450.00)
o/w NASSIT	-	-	-	-	-
182 DAYS TBs	**1,996.60**	**4,671.85**	**5,039.65**	**2,675.25**	**367.80**
BSL	-	-	12.80	-	12.80
COMM. BANKS	-	-	-	-	-
NON-BANK PUBLIC	1,996.60	4,671.85	5,026.85	2,675.25	355.00
o/w NASSIT				-	-
364 DAYS TBs	**8,405,878.40**	**8,827,757.10**	**9,362,182.00**	**421,878.70**	**534,424.90**
BSL	569,117.40	589,718.10	1,168,683.05	20,600.70	578,964.95
COMM. BANKS	6,691,656.25	7,157,916.95	7,017,113.65	466,260.70	(140,803.30)
NON-BANK PUBLIC	1,145,104.75	1,080,122.05	1,176,385.30	(64,982.70)	96,263.25
o/w NASSIT	*55,500.00*	*59,051.65*	*64,051.65*	3,551.65	5,000.00
1.5 YR T BONDS	**-**	**-**	**-**	**-**	**-**
BSL	-	-	-	-	-
COMM. BANKS	-	-	-	-	-
NON-BANK PUBLIC	-	-	-	-	-
o/w NASSIT	-	-	-	-	-
2 YR T BONDS	**317,597.85**	**471,829.20**	**471,829.20**	**154,231.35**	**-**
BSL	-	-	-	-	**-**
COMM. BANKS	257,110.85	401,342.20	401,342.20	144,231.35	**-**
NON-BANK PUBLIC	60,487.00	70,487.00	70,487.00	10,000.00	-
o/w NASSIT	*60,487.00*	*70,487.00*	70,487.00	10,000.00	-
TOTAL MARKETABLE	**8,725,472.85**	**9,504,117.30**	**9,840,284.75**	**778,644.45**	**336,167.45**
BSL	569,117.40	787,893.35	1,168,695.85	218,775.95	380,802.50
COMM. BANKS	6,948,767.10	7,559,259.15	7,418,455.85	610,492.05	(140,803.30)
NON-BANK PUBLIC	1,207,588.35	1,156,964.80	1,253,133.05	(50,623.55)	96,168.25
o/w NASSIT	*115,987.00*	*129,538.65*	*134,538.65*	13,551.65	5,000.00
3 YR T BONDS	**345,929.40**	**424,792.10**	**701,967.35**	**78,862.70**	**277,175.25**
BSL	227,382.80	227,382.80	425,558.05	-	198,175.25
COMM. BANKS	93,546.60	172,409.30	251,409.30	**78,862.70**	**79,000.00**
NON-BANK PUBLIC	25,000.00	25,000.00	25,000.00	-	-
o/w NASSIT	*25,000.00*	*25,000.00*	25,000.00	-	-
5 YR T BONDS	**367,989.80**	**367,989.80**	**367,989.80**	**-**	**-**
BSL	326,918.00	326,918.00	326,918.00	-	-
COMM. BANKS	-	-	-	-	-
NON-BANK PUBLIC	41,071.80	41,071.80	41,071.80	-	-
o/w NASSIT	*41,071.80*	*41,071.80*	41,071.80	-	-
10 YR T BONDS	**18,750.00**	**18,750.00**	**15,000.00**	**-**	**(3,750.00)**
BSL	18,750.00	18,750.00	15,000.00	**-**	(3,750.00)
COMM. BANKS	-	-	-	**-**	-
NON-BANK PUBLIC	-	-	-	**-**	-
o/w NASSIT	-	-	-	**-**	-
TOTAL NON-MARKETABLE	**732,669.20**	**811,531.90**	**1,084,957.15**	**78,862.70**	**273,425.25**
BSL	573,050.80	573,050.80	767,476.05	**-**	194,425.25
COMM. BANKS	93,546.60	172,409.30	251,409.30	78,862.70	79,000.00
NON-BANK PUBLIC	66,071.80	66,071.80	66,071.80	**-**	-
o/w NASSIT	*66,071.80*	*66,071.80*	*66,071.80*	**-**	-
TOTAL GOV. SECURITIES	**9,458,142.05**	**10,315,649.20**	**10,925,241.90**	**857,507.15**	**609,592.70**
BSL	1,142,168.20	1,360,944.15	1,936,171.90	218,775.95	575,227.75
COMM. BANKS	7,042,313.70	7,731,668.45	7,669,865.15	689,354.75	(61,803.30)
NON-BANK PUBLIC	1,273,660.15	1,223,036.60	1,319,204.85	(50,623.55)	96,168.25
o/w NASSIT	182,058.80	195,610.45	200,610.45	13,551.65	5,000.00