Bank of Sierra Leone

Governor's Office

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30 September 2019

MONETARY POLICY STATEMENT

The Monetary Policy Committee (MPC) of the Bank of Sierra Leone met on 26th September 2019 under the Chairmanship of the Governor, Professor Kelfala M. Kallon, and decided to keep the Monetary Policy Rate (MPR) unchanged at 16.5 per cent. The decision was based on its assessment of recent global and domestic macroeconomic developments and expected trends in key macroeconomic variables that are related to the Bank's core mandate of price and financial stability. The evidence underlying the Committee's decision are as follows.

Inflation Forecast

According to preliminary data on the Consumer Price Index provided by Statistics Sierra Leone, headline inflation declined from 14.8 per cent in March 2019 to 14.7 per cent in June 2019. It, however, picked up slightly to 15.4 per cent in August 2019. This was, in part, due to the effect of the rainy season on food prices, on the one hand, and the impact of increased foreign-exchange demand caused by both increased food imports and the Hajj pilgrimage, on the other hand.

However, the expected slowdown in the global economy in 2019 (due to the escalating trade war between the US and China, Brexit-related uncertainty and sluggish global trade) could dampen global commodity demand. This would then depress global commodity prices (particularly crude oil and PLATT), thereby softening domestic inflationary pressures. Furthermore, the MPC expects the ongoing fiscal consolidation measures of Government to continue, thereby dampening domestic inflationary pressures. Also, increased domestic food production in the harvest season is likely to depress food-price inflation. Consequently, in spite of the observed seasonal inflationary spike in August 2019, the MPC expects inflation to decline in the next quarter of the year.

Global Economic Growth

The global economy weakened during the third quarter. Consequently, global economic growth for 2019 has been revised downward to 3.2 per cent, from the IMF's earlier projection of 3.3 percent (IMF WEO July 2019). It is, however, expected to rebound to 3.6 percent in 2020, although the probability of actual growth falling short of this expectation remains high. More specifically, because China is Sierra Leone's main trading partner, any adverse shock on its economy will likely profoundly impact Sierra Leone's economy.

Domestic Economic Growth

Domestic real GDP growth is projected to pick up from 3.3 per cent in 2018 to 5.1 percent in 2019. This is expected to be largely driven by improvements in agricultural production and continued growth in public investment in infrastruture and human capital. The Bank of Sierra Leone's Composite Index of Economic Activity (CIEA) shows that domestic economic activity picked up in the second and third quarters. The MPC expects this to continue in the fourth quarter and, therefore, expects the predicted 5.1 percent real GDP growth to materialize during the year. We, however, caution that this prediction assumes that the temporary suspension of iron-ore exports by Government would be short lived. Otherwise, it could cause actual real GDP growth to fall below expectation.

Fiscal Policy

Fiscal operations resulted in a budget surplus during the second quarter of 2019. This was primarily due to Government's fiscal consolidation efforts, which we expect to continue in the fourth quarter. Specifically, domestic revenues exceeded their targeted level, while expenditures remained within the budget ceiling for the third quarter. Despite these developments, the currently high level of accumulated arrears and debt service payments will continue to pose challenges for the fiscal balance.

Money and Banking

Reflecting both increased fiscal consolidation and weak aggregate demand, broad money supply (M2) growth moderated and remains within the target under the ECF program with the IMF. The MPC noted that credit to the private sector improved, but it is still below its projected target under the ECF program. This is primarily due to high interest rates on Treasury Bills, which causes banks to concentrate on lending to Government instead of the private sector. High credit risk of lending to the private sector also compounds the problem.

In the money market, liquidity remains tight, as evidenced by the persistent undersubcriptions in the primary market for government securities and increased frequency of commercial banks access to the BSL's standing lending facility. Furthermore, although the interbank rate remained within the interest rate corridor, it continues to trend above the MPR, reflecting the tight liquidity in the money market.

The banking sector remains relatively stable, as evidenced by improvements in the key financial soundness indicators. However, the non-performing loans ratio, though declining, remains slightly above the prudential limit.

The Exchange Rate

The depreciation of the Leone against major currencies continued in the second and third quarters of the year. This reflects continued excess demand for foreign currency, which is primarily due to weak export performance and strong import demand. Additionally, the persistent depreciations created expectations of future depreciations, which then intensified the hoarding of foreign currency for speculative purposes.

The commercial banks, also, did not help the situation by their unwillingness or inability to pay holders of foreign currency accounts in foreign currency on demand. Additionally, the service fees commerical banks charge for official foreign exchange transactions are quite unjustifiably exhorbitant. These caused banks to lose their comparative advantage in foreign exchange transactions, thereby creating space for the parallel market to exploit.

However, the anticipated increase in foreign exchange inflows from the resumption of iron ore exports, foreign direct investments, and disbursements from development partners, as well as the impact of the temporary measures that have been put in place by the Bank of Sierra Leone to rechannel foreign currency transactions through the formal market should ameliorate the problem.

Conclusion

Based on the forecasted deceleration of inflation for the remainder of the year, as well as the need to support economic growth, the MPC decided to keep the Monetary Policy Rate, the Standing Lending Facility Rate, and the Standing Deposit Facility Rate unchanged. The public should rest assured, however, that should any development adversely impact inflationary expectations, the Committee will respond appropriately.

Hence, effective 30th September 2019, the following rates are published for the information of the public:

Monetary Policy Rate is 16.5 per cent
Standing Deposit Facility Rate is 13.5 per cent
Standing Lending Facility Rate is 20.5 per cent

Professor Kelfala M. Kallon
Governor