BANK OF SIERRA LEONE

MONETARY POLICY REPORT

MARCH 2024

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ACRONYMS

AE	Advanced Economies
BOP	Balance of Payments
BSL	Bank of Sierra Leone
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
GoSL	Government of Sierra Leone
GST	Goods and Services Tax
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
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

The Report

The March 2024 edition of the BSL Monetary Policy Report presents an assessment of global and domestic economic developments, mainly during the fourth quarter of 2023. The report also assesses current developments in the first quarter of 2024 for which data is available, as well as near-term prospects, with a view to implementing appropriate monetary policy consistent with the Bank's policy objectives.

BSL Monetary Policy Objectives

The primary objective of the BSL 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 (MPR), 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 Stability, 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 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, selected MPC members and staff of relevant policy departments engage markets participants notably the commercial banks 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.

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[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.*

EXECUTIVE SUMMARY

The global economy has proven to be remarkably resilient to shocks in recent years. This resilience is mostly due to strong macroeconomic fundamentals in most Advanced and Emerging market economies and robust consumer and government spending. Also, labor markets have held up and supply chains have normalized, coupled with decreasing food and energy prices. Growth for 2024 is projected to increase by 3.1 percent (Jan. WEO, 2024), a 0.2 percentage points upgrade from the October 2023 WEO projections. Furthermore, global growth is estimated to edge up to 3.2 percent in 2025. On the other hand, Global inflation has been declining faster than anticipated across most regions. This is attributed partly to improvements in global supply chain conditions and the effects of previous tight policy stances by central banks. As a result, global inflation, previously estimated at 6.8 percent in 2023, is projected to moderate to 5.8 percent in 2024.

On the domestic economy, the real GDP growth is projected to increase to 4.7 percent in 2024 and 5.2 percent in 2025, from a subdued growth of 2.7 percent in 2023. The projected growth in GDP could be driven by increased investment in agriculture, mining activities, and a recovery in the services sector. Furthermore, the Bank’s analytical high frequency indicator i.e., the Composite Index of Economic Activities (CIEA), recorded a positive growth in economic activity in 2023Q4 compared to a contraction in 2023Q3. This reflects increase in exports, and currency in circulation, while growth in capital expenditure moderated.

On the external front, the trade deficit with the rest of the world narrowed by 50.9 percent to US$111.3mn in 2023Q4 from US$226.6mn in the previous quarter, reflecting the combined effects of an increase in exports receipts and a reduction in import bills. The gross international reserves of the BSL increased in 2023Q4 and was equivalent to 2.7 months of import of goods and services, above the 2.3 months of import of goods and services recorded in 2023Q3. Inflows from development partners helped boost the reserve position of the BSL. The exchange rate has remained relatively stable over the last nine months, due to policy measures implemented by the BSL to address challenges in the foreign exchange market. Market participants also note a decrease in speculative behaviour and currency substitution, indicating increased confidence in the BSL's policies.

In the monetary sector, both Reserve Money (RM) and Broad Money (M2) increased nominally in 2023Q4 compared to 2023Q3. RM expanded due to an increase in the Net Domestic Assets (NDA) of the BSL, while M2 growth was driven by the NDA of the Banking System, primarily due to an increase in holdings of government securities. However, both RM and broad money growth declined in real terms. Additionally, credit to the private sector by commercial banks increased nominally in 2023Q4 compared to the previous quarter but showed a significant real contraction.

In the money market, the yield on the 364-day T-bills increased steadily in 2023Q4 and continued its upward trend, reaching a peak of 39.5 percent in February 2024. Meanwhile, the 91-day and 182-day T-bill markets remained illiquid. Demand for government treasury bills remained skewed towards the 364-day tenure, with deposit money banks being the primary participants. Additionally, the interbank market rate continued its upward trajectory, nearing the overnight lending facility rate, indicating tight liquidity conditions.

The financial sector remained relatively stable, with most key Financial Soundness Indicators (FSIs) within acceptable thresholds. The stability is on account of BSL's strengthened regulatory and prudential oversight, and the strong banking system profitability generated from the significant investment in government securities. Despite the overall stability, inherent risks persist, including limited intermediation for growth support, a high level of non-performing loans (NPLs), interest rate risks stemming from heavy reliance on government securities for banking sector earnings, cyber security threats, and risks associated with information technology. A sudden and large drop in T-bill rates poses a significant interest rate risks to bank profitability and capital positions, potentially impacting lending activity adversely. Conversely, a gradual decline in rates may incentivise banks to explore new lending opportunities.

The government's budgetary operations shifted from a deficit of NLe2.4bn in 2023Q3 and NLe2.6bn in 2023Q2 to a surplus of NLe0.4bn in 2023Q4. This improvement was driven by increased foreign grants, enhanced revenue collection, and reduced expenditure. Consequently, the primary balance showed a surplus of NLe0.3bn in 2023Q4, contrasting with a deficit of NLe1.3bn in 2023Q3.

Inflation declined steadily from 54.6 percent in October 2023 to 42.6 percent in February 2024, driven by decreases in both food and non-food prices. This reduction can be attributed to the Bank's tight monetary policy stance, exchange rate stability, increased food supply during the harvest season, stable fuel prices, and base effect in the Consumer Price Index (CPI).

However, there are potential upward pressures on the inflation forecast. These include the immediate effects of the proposed fiscal measures in the 2024 Finance Act, which may lead to direct and indirect price increases. Additionally, there's volatility in energy prices due to the ongoing reduction in production by the Organization of Petroleum Exporting Countries (OPEC), alongside elevated inflation expectations.

The rest of the report is organised as follows: The second section analyses the 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 MPC members at the MPC meeting held in March 2024.

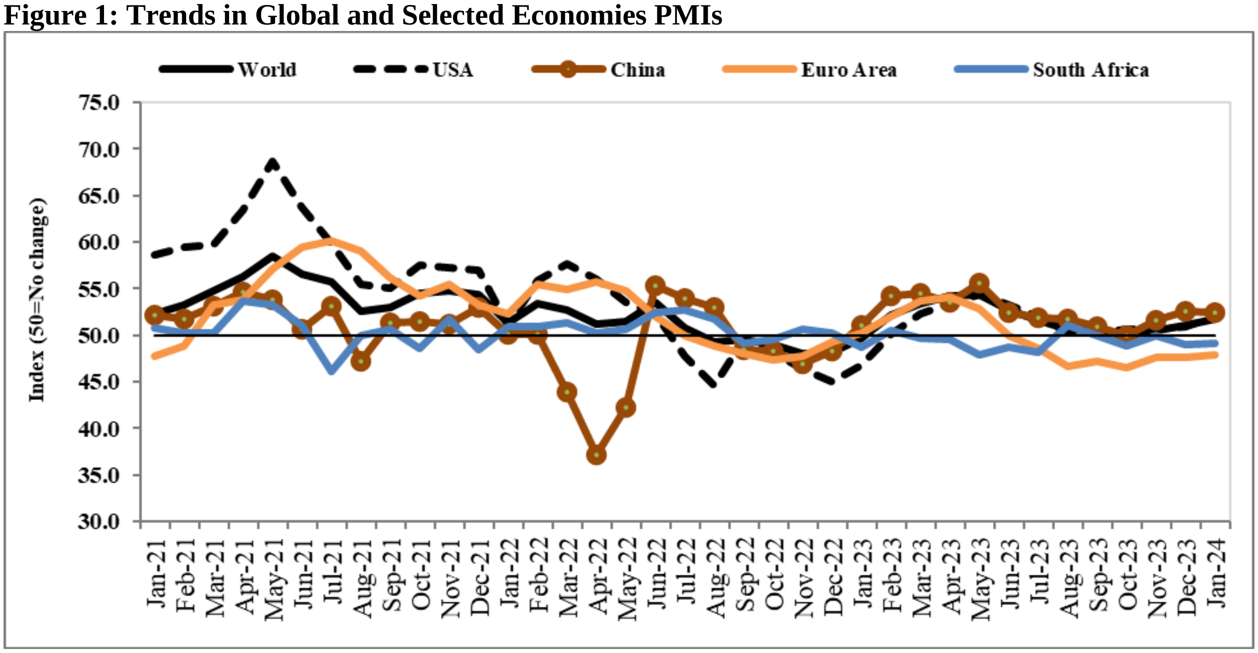
1. GLOBAL ECONOMIC DEVELOPMENTS AND PROSPECTS

1.1 Global Output

The global economy remained resilient in 2023Q4, with growth holding up. However, the pace of the progress in growth remains slow and potential drawbacks may lie ahead. Unwinding supply chains, decreasing food and energy prices, as well as the slight pickup of economic activity in China are boosting global economic activity and sentiments. However, the Composite Purchasing Managers' Indices (PMI) indicates that even though economic activity picked up in China,economic performance has been marked by volatility, ongoing deflationary pressures, and still weak consumer confidence. Some improvement was observed in the United States, as the composite PMI rose through December 2023.

The Euro Area is anticipated to avoid a double-dip recession in 2024, as the PMI continues to signal expansion in economic activity. Moreover, the global composite PMI is driven by the services sector, due to ease in lockdown measures and the pent-up consumer demand. The manufacturing sector activity remained subdued, mainly due to headwinds from higher input costs,supply chain disruptions and tighter monetary policy.

Figure 1: Trends in Global and Selected Economies PMIs



Data Source: Markit Economics, through Trading Economics January 4, 2024. Note: PMIs above 50% signals expansion in economic activity; below 50% signals contraction

Notwithstanding the positive signals suggested by the composite PMIs, high interest rates, escalation of the Russia-Ukraine war, US- China tensions, financial stress risks, weak trade, Israel-Palestine war, and unsettled political conditions in the Red Sea region could weigh on global growth going forward. In addition, difficult policy trade-offs and increasing debt distress in many emerging markets and developing economies across the world could serve as major headwinds for economic growth going forward. However, the IMF forecast for 2024 growth is about 0.2 percentage point higher, reflecting upgrades for China, the United States, and large emerging market and developing economies.

1.1.1 Advanced and Emerging Market Economies

Economic activities in advanced economies deteriorated slightly, as the impact of the banking crisis and the tightening of monetary policy have dampened consumer and business confidence. Consumption and investment growth have slowed down, while inflation remains elevated. As a result, growth in advanced economies is expected to stay sluggish at 1.5 percent in 2024 after 1.6 percent in 2023.

There was a modest pickup of activity in emerging market and developing economies supported in part by expansion of services and spillovers from resilient growth in the United States. However, they also face headwinds from higher interest rates, weaker external demand, and supply disruptions. In China, weaker consumption and investment continue to weigh on activity. Consequently, growth in emerging markets and developing economies is projected to increase slightlyto 4.2 percent in 2024 from 4.1 percent in 2023.

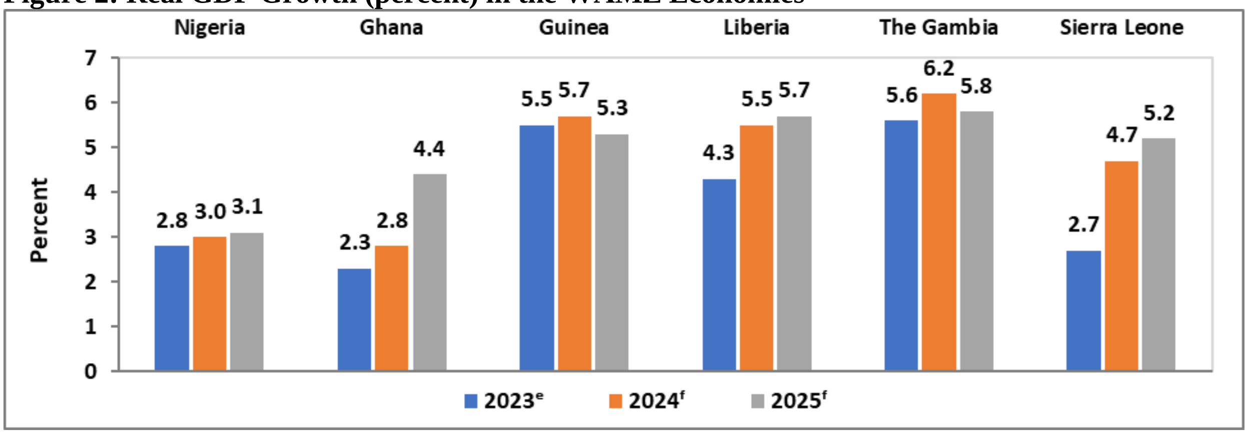
1.1.2 Sub-Saharan Africa

Growth momentum in Sub-Saharan Africa remained moderate in the last quarter of 2023. Weak economic outturn in South Africa and Nigeria is expected to offset improvement across most of the region. However, the region is projected to remain broadly resilient with stable outlook through 2024. In this regard, growth in the region is projected to improve to 3.8 percent in 2024 from 3.3 percent in 2023.

1.1.3 West African Monetary Zone (WAMZ)

Overall, economic activities in the WAMZ bloc experienced a subdued growth in 2023Q4, mainly driven by weak performances in Nigeria and Ghana, the two largest economies in the bloc. They are expected to register lower growth rates than in the previous quarters, due to weak consumer demand, low oil prices, and fiscal constraints. Liberia and Sierra Leone are also likely to face headwinds from infrastructure gaps, and environmental shocks, but growth in Sierra Leone is expected to be supported by a pick-up in mining, agriculture and services. The Gambia and Guinea are forecasted to maintain robust growth levels, supported by recovery in the services sector and mining sector, respectively. Looking ahead, overall performance in the bloc is expected to improve in 2024, although growth will remain below historical levels in most economies.

Figure 2: Real GDP Growth (percent) in the WAMZ Economies



Source: IMF World Economic Outlook, October 2023, and January 2024 update; Note: e=estimate and f =forecast

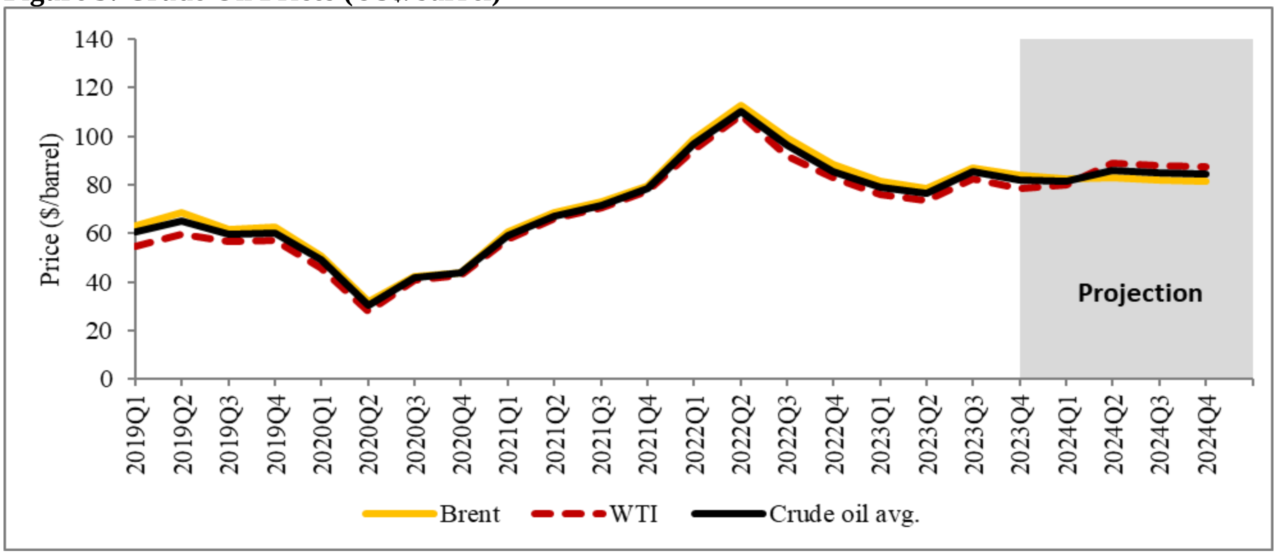
1.2 Global Commodity Prices and Inflation

1.2.1 Global commodity prices

Crude Oil Prices

Crude oil prices declined further in 2023Q4, reaching their lowest level since 2020. The average crude oil price was US$81.20/bbl, down by 4.8 percent from 2023Q3 and 23.6 percent from the peak in 2022Q2. The main drivers of this downward trend are the persistent weak demand due to the global economic slowdown and the over-supply from Russia and OPEC+. Brent and WTI crude oil prices follow a similar pattern, with brent dropping to US$84.0/bbl and WTI to US$78.4/bbl in 2023Q4. Crude oil prices are expected to stay around current levels in the short run.

Figure 3: Crude Oil Prices (US$/barrel)

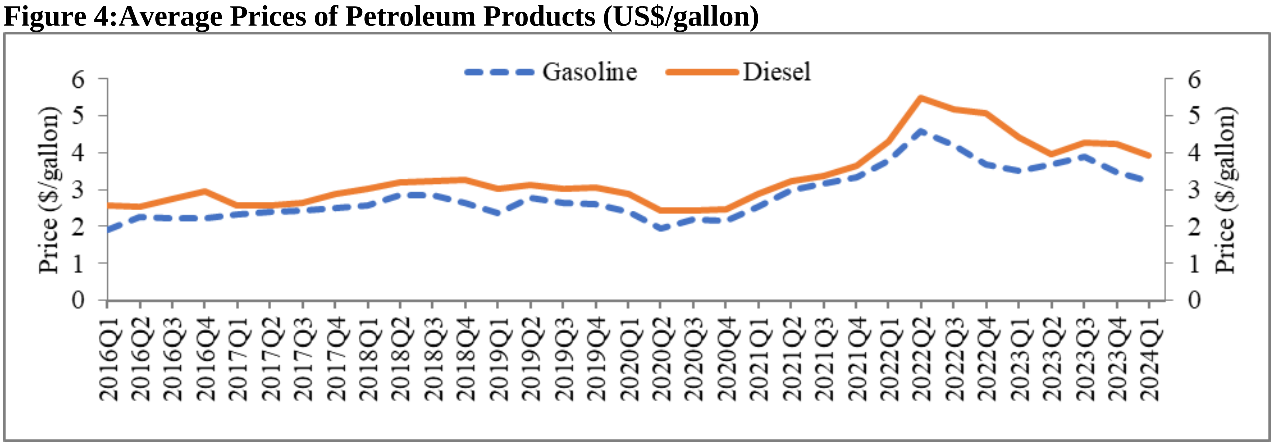


Source: World Bank Commodity Market Database January 2024

Petroleum Products (Retail Prices)

Global petroleum prices continued to decrease in 2023Q4 mainly reflecting the decline in crude oil prices, and the slow recovery of demand from the pandemic, and U.S. dollar remains weak as the Federal Reserve maintains itsaccommodative monetary policy stance.

Figure 4:Average Prices of Petroleum Products (US$/gallon)

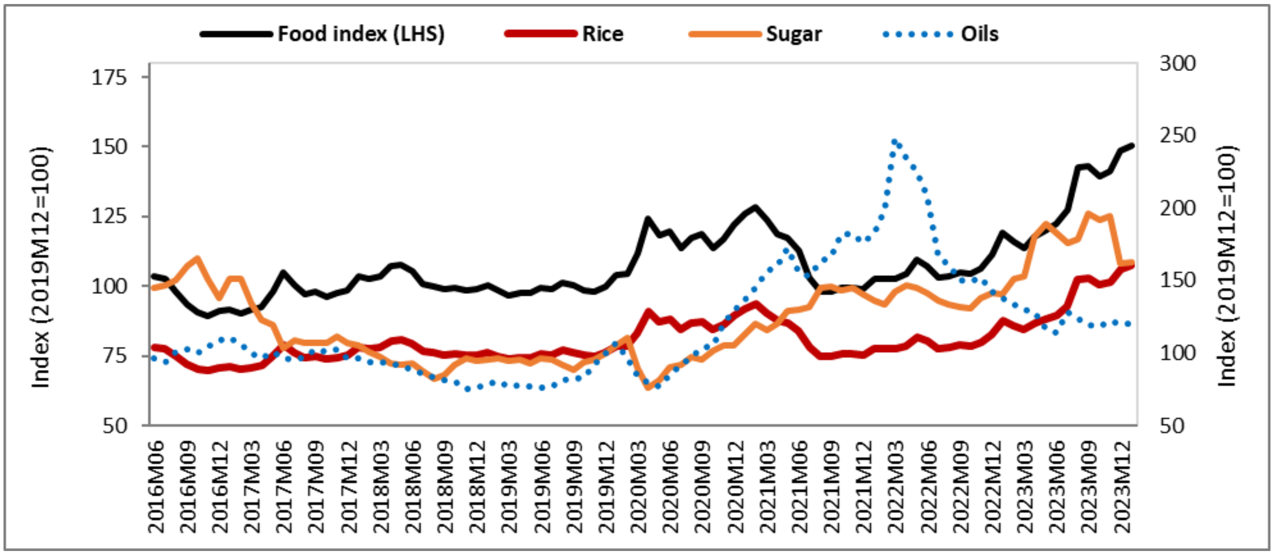


Source: U.S. Energy Information Administration, EIA (January 2024)

Food Price Index

Despite the ongoing decreases in the FAO global food price indices, the prices of food commodities imported into Sierra Leone continue to rise, as reflected by the estimates of imported food price index by the Bank of Sierra Leone (BSL). This rise is primarily due to rising prices of rice, which is the most important staple food and food import item in Sierra Leone.

Figure 5:BSL's Estimated Import Food Price Index

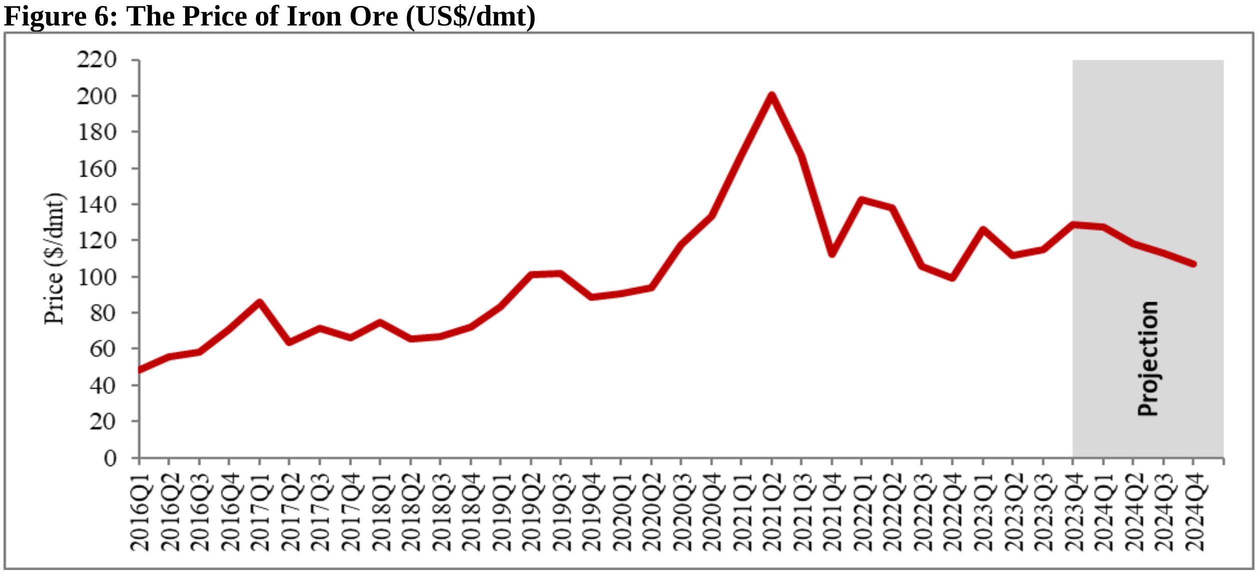


Source: BSL Staff estimation using data from the World Bank Commodity Market database, January 2024.

Iron Ore Price

Iron ore prices rebounded by 12 percent in 2023Q4, reaching a level of 129.0 dollars per tonne. This increase was driven by a recovery in China's steel production, which boosted the demand for iron ore. However, this effect is likely to be temporary, as China faces environmental pressures and trade tensions that may limit its steel output held up over the remainder of 2024. Consequently,iron ore prices are projected to decline again in 2024.

Figure 6: The Price of Iron Ore (US$/dmt)

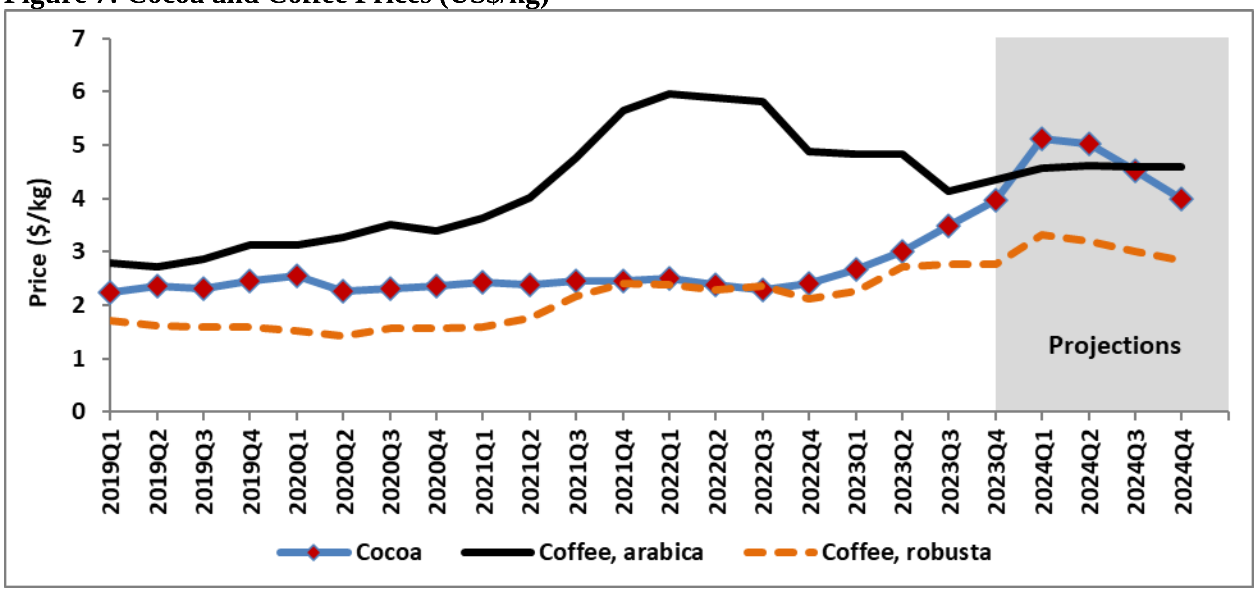


Source: World Bank Commodity Market Database January 2024

Cocoa and Coffee Prices

Cocoa prices continued to rise by double digits, i.e. by 13.5 percent, selling at US$4.21/kg in December 2023, driven by strong demand from chocolate manufacturers and lower production in West Africa. Cocoa prices extended their steep rise by increasing another 32 percent in the first two months of 2024, reaching US$5.56/kg. Average robusta coffee prices stayed flat, selling at US$2.77/kg in 2023Q4 due to lower exports from Vietnam and Indonesia, and higher demand from roasters. Arabica coffee prices, however, increased by 4.9 percent, selling at US$4.35/kg on average in 2023Q4, as the Brazilian crop recovered from the previous drought and the Colombian peso depreciation. Cocoa prices are projected to fall in 2024, as supply and demand balance out and weather conditions improve while coffee prices are expected to stay around end-2023 levels.

Figure 7: Cocoa and Coffee Prices (US$/kg)



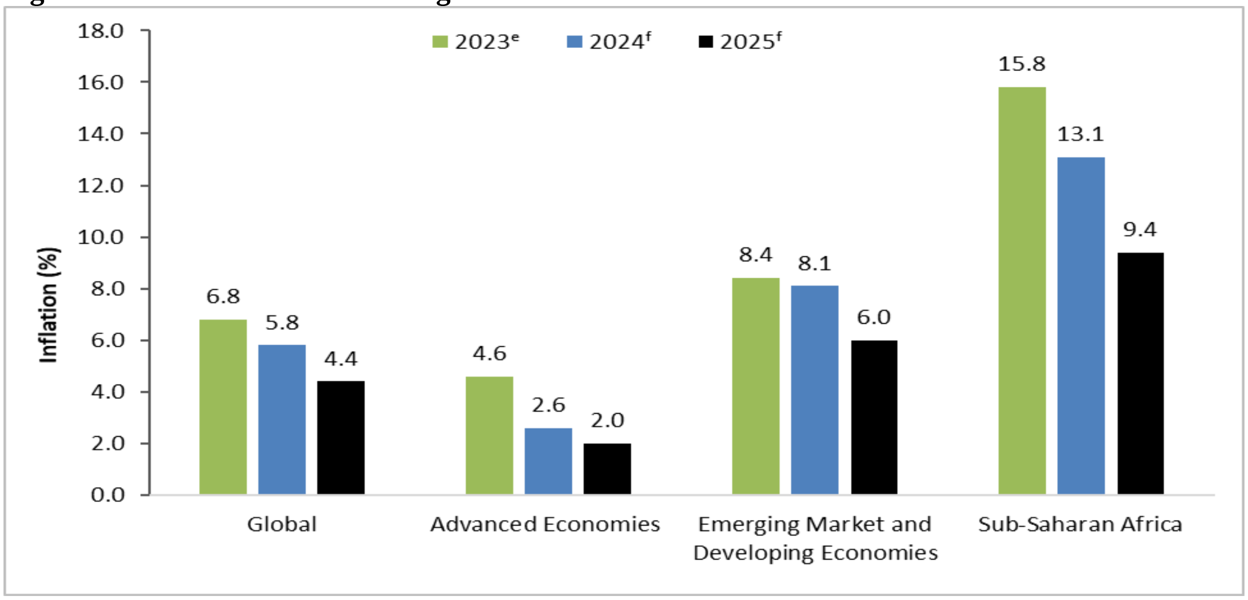
Source: World Bank Commodity Market Database January 2024

1.2.2 Global Inflation

Global inflation is estimated at 6.8 percent in 2023. However, inflation in recent months has been declining faster than anticipated across most regions. As a result, global inflation is projected to moderate to 5.8 percent in 2024. This slowdown in inflation reflects continued tight monetary policy across major economies, as well as an improvement in supply chain conditions and a decline in commodity prices. Nevertheless, core inflation remains elevated in many regions, especially in emerging markets and developing economies (EMDEs), where financial vulnerabilities and exchange rate pressures pose significant risks.

According to the IMF Jan 2024 WEO, inflation in advanced economies was estimated at 4.6 percent in 2023, while inflation in EMDEs remained at 8.4 percent. Among the latter group, sub-Saharan Africa faces the highest inflation rate of 15.8 percent, driven by persistent food insecurity, currency depreciation and fiscal imbalances.

Figure 8: Trends in Global and Regional Inflation



Source: IMF World Economic Outlook (WEO), Jan. 2024 and Oct. 2023

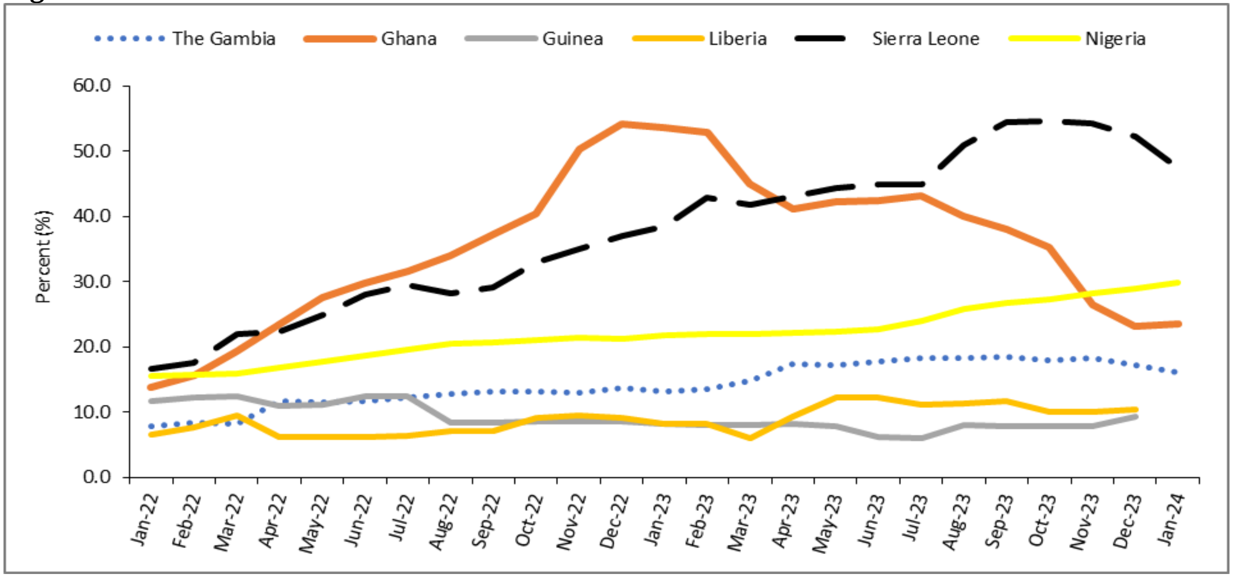
Sub-Saharan Africa (SSA) Inflation

Inflation in Sub-Saharan Africa reached 15.8 percent in 2023Q4, the highest level since 1994. This was mainly driven by supply shocks, currency depreciation, and fiscal expansion in some of the largest economies in the region, such as Nigeria, Ethiopia, and Angola. The outlook for 2024Q1 is also bleak, as inflation is projected to remain above 13.0 percent, well above the target range of most central banks, compared to October 2023 WEO, due to persistent underlying inflationary forces.

Inflation in the WAMZ

The WAMZ economies experienced high consumer price inflation in the last quarter of 2023, except for Guinea and Liberia which maintained stable inflation rates. The most notable change was the significant drop in Ghana's inflation, which reached a low of 23.2 percent in December 2023. Ghana’s reduced inflation rate is associated with factors such as tighter monetary policy, lower currency depreciation, and reduced fuel prices. The other countries in the bloc also saw some moderation in inflation, but not as dramatic as Ghana's. The situation in Sierra Leone resembles that of Ghana with a one-year lag, which supports a positive domestic inflation outlook.

Figure 9: Inflation Trends in the WAMZ



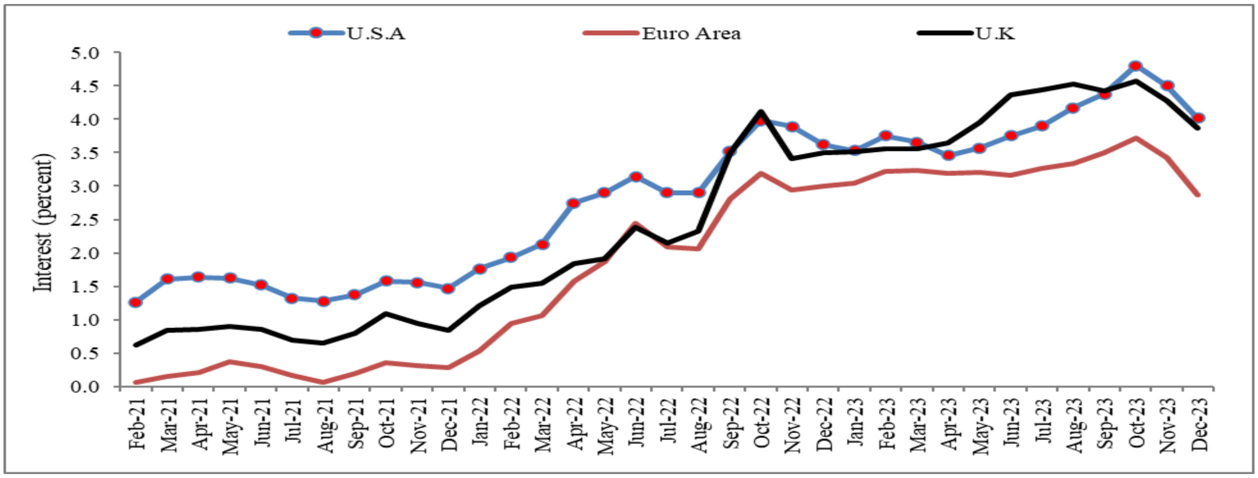
Data Source: Country Central Banks through Trading Economics

1.3 Monetary Policy and Financial Market Developments

Global financial conditions remain tight. Although global inflation is decelerating, it remains high in most countries and the outlook is also clouded with uncertainties due to geopolitical tensions such as the Israel-Palestine conflict, Russian-Ukraine war, renewed supply chain disruptions and increased shipping costs.

The monetary policy authorities faced a difficult trade-off between fighting inflation and supporting growth and financial stability. Some central banks, such as those in the WAMZ region, increased their policy rates significantly to curb inflation and defend their currencies, while others, such as those in the major economies, adopted a more cautious approach and kept their policy rates unchanged or raised them slightly.

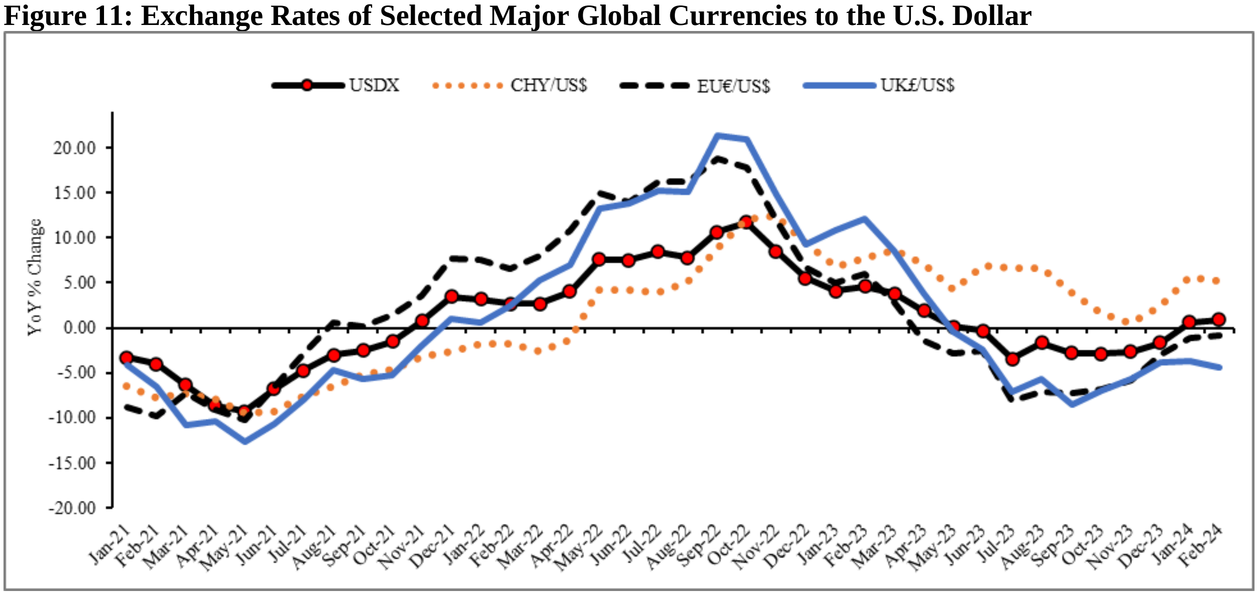
Figure 10: Selected Sovereign Bond Yields



Source: Federal Reserve Economic Data (FRED) December 2023

The global financial conditions eased somewhat but continued to be tight, as the interest rates on the 10-year government bonds in the United States, Euro Area and United Kingdom remained high in 2023Q4. This kept the borrowing costs and debt burdens high for many emerging markets and developing economies, especially those with high external debt and weak fiscal positions. The global uncertainty also dampened the investment and consumption sentiments, leading to lower growth prospects for 2024.

Figure 11: Exchange Rates of Selected Major Global Currencies to the U.S. Dollar



Data Source: FRED (January 2024) Note: a positive change indicate depreciation against the U.S. dollar and a negative change indicates an appreciation against the U.S. dollar.

1.4 Implications of the Global Developments for the outlook of the Sierra Leone economy

The lower global commodity prices, as well as the improved global supply chains, could reduce the cost and volume of Sierra Leone's imports, leading to a lower current account deficit and less pressure on the domestic currency.

The subdued global inflation could also lower the pass-through effect of imported inflation for Sierra Leone in the near future.

The increased demand for Sierra Leone's exports, especially iron ore and cocoa, could support higher GDP growth and generate more foreign exchange earnings.

However, some downside risks remain, such as the tight global financial conditions that could limit the inflow of FDI and ODA to the country. Moreover, the high global uncertainty could negatively affect domestic economic activity in 2024.

The challenging economic conditions in China, including deflationary pressures, could drag the growth of the Sierra Leone economy.

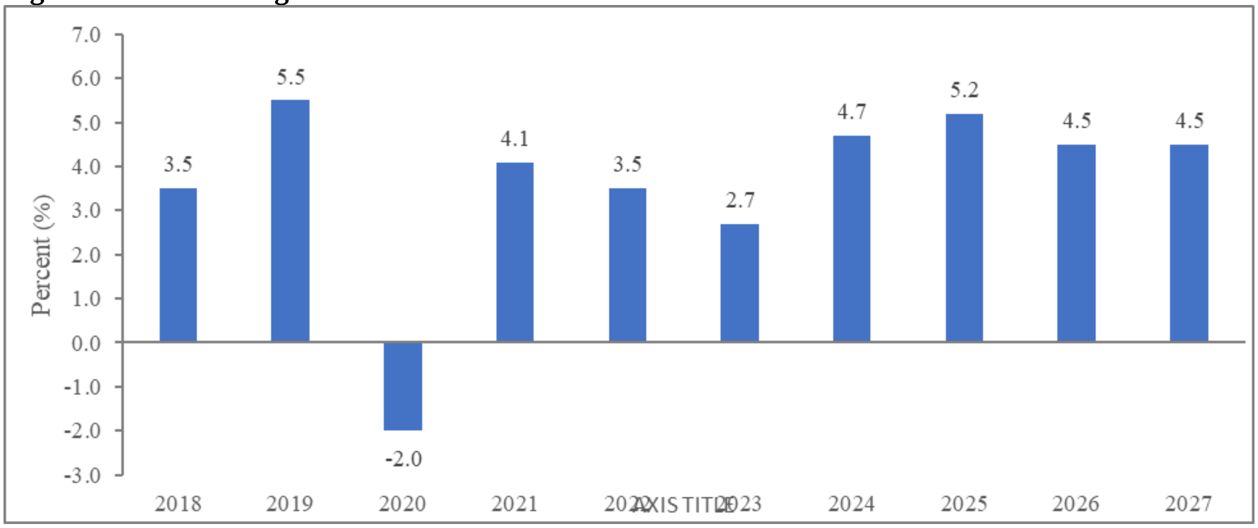
2.0 DOMESTIC ECONOMIC DEVELOPMENTS

2.1 Real Sector Development

2.1.1 Real GDP Growth

Growth in Real GDP is projected to rebound to 4.7 percent in 2024 and 5.2 percent in 2025, compared to an estimated subdued growth of 2.7 percent in 2023. The expected strong growth momentum will be driven by robust growth in agriculture and mining, an upturn in the services sector, and investment in essential infrastructure while continued fiscal tightening will remain a drag. Growth is expected to remain resilient over the medium term reflecting continued macroeconomic stability. However, risks to the projection are tilted to the downside due to potentially larger policy interventions by the government, renewed depreciation of the Leone, as well as global supply chain disruptions since the onset of the geo-political conflict in Europe and the Middle East.

Figure 12: Real GDP growth



Source: Statistics Sierra Leone & IMF

Excluding iron ore and mining sector, real GDP growth is projected to increase to 4.6 percent and 5.0 percent in 2024 and 2025, respectively, from a weak growth rate of 2.6 percent in 2023. In 2025, both real GDP growth excluding iron ore and mining sector will remain strong at 5.0 percent and 4.7 percent respectively.

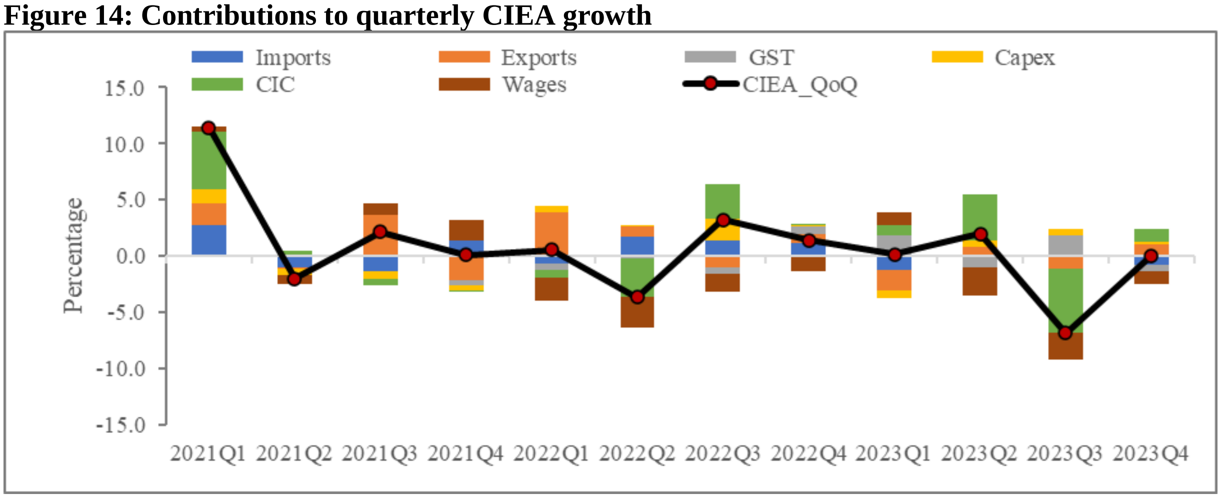
Figure 13: Real GDP growth Rates Excluding Iron ore and Mining Sectors

Source: Statistics Sierra Leone & IMF

2.1.2 Composite Index of Economic Activity (CIEA)

The Bank's analytical high frequency indicator, the Composite Index of Economic Activities (CIEA) recorded a positive growth in economic activity in 2023Q4 compared to a sharp contraction in 2023Q3. The positive growth in the CIEA reflects increase in exports, and currency in circulation, while growth in capital expenditure moderated. However, imports, wages and salaries, and goods and services tax decreased in the reviewed quarter.

Figure 14: Contributions to quarterly CIEA growth

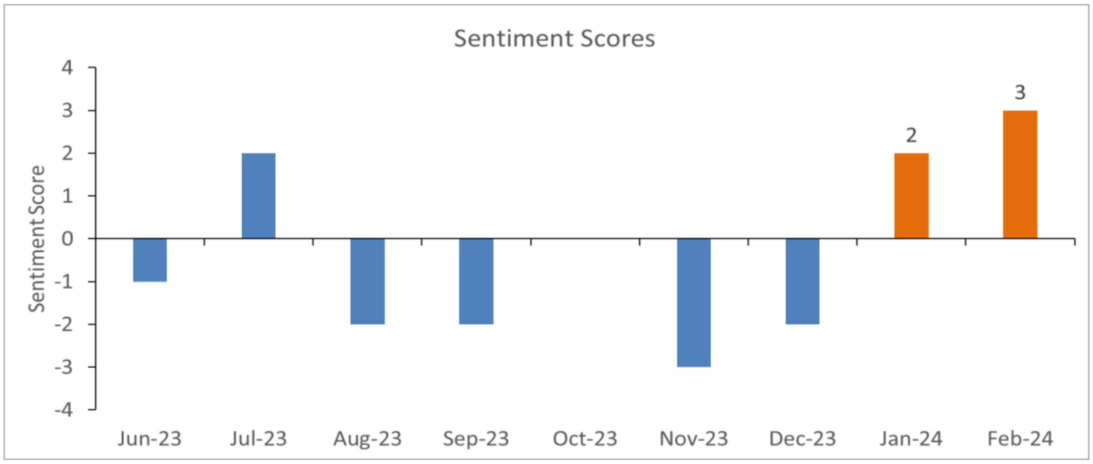


Source: Bank of Sierra Leone (BSL)using The Conference Board approach

Box 1: Business Confidence[2]

The Bank's business sentiment scores were 2 and 3 in the months of January and February 2024, respectively. These scores point to a positive business perception, indicating that businesses are generally optimistic and confident regarding their current and near future economic conditions.

Figure 15: Business Sentiment Scores



Source: BSL, staff calculation

2.1.3 Price Developments

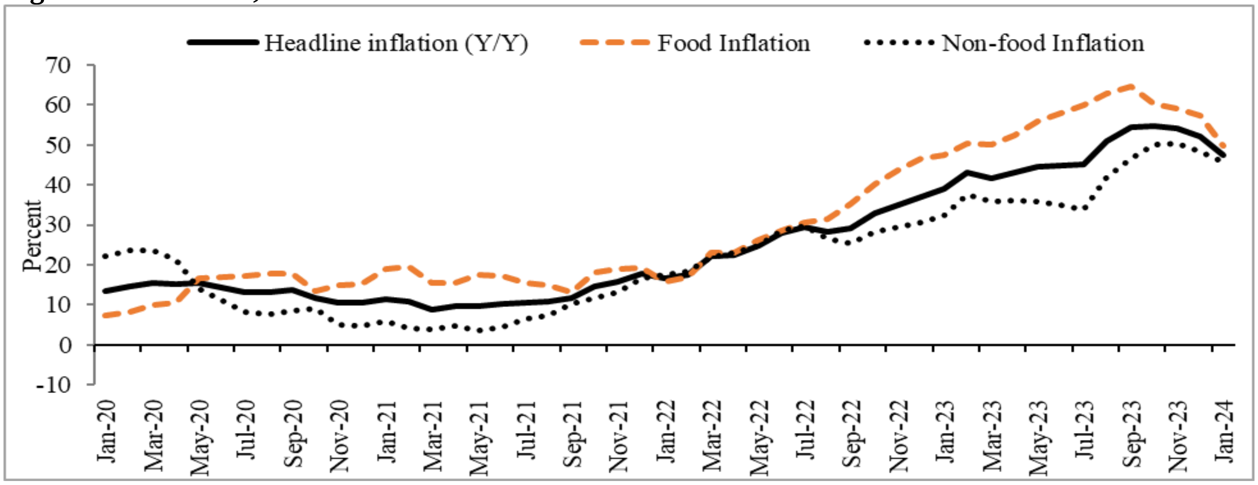
Inflationary pressures have been easing since October 2023. Headline inflation decreased from 54.6 percent in October 2023 to 52.2 percent in December 2023. Inflation further declined to 47.4 percent in January and then to 42.6 percent in February 2024 due to a decline in prices of both food and non-food components of the consumer basket.

Increase in domestic food supply during the harvest season partly explains the decrease in the volume of goods imported into Sierra Leone (with associated decrease in imported inflation). Imports of food, vegetable oil, and manufacturing goods decreased in both volume and value in January 2024. Hence, food inflation dropped to 49.8 percent in January 2024 from 57.2 percent in December 2023. Non-food inflation fell to 45.6 percent in January 2024 from 48.3 percent in December 2023.

At the policy level, the decrease in inflation is supported by the impact of the tight monetary policy of the bank, a relatively stable exchange rate coupled with adjustment in the GST tax brackets for SMEs and expenditure rationalization of the government contributed to the recent decline in headline inflation.

[2] The business confidence is still experimental.

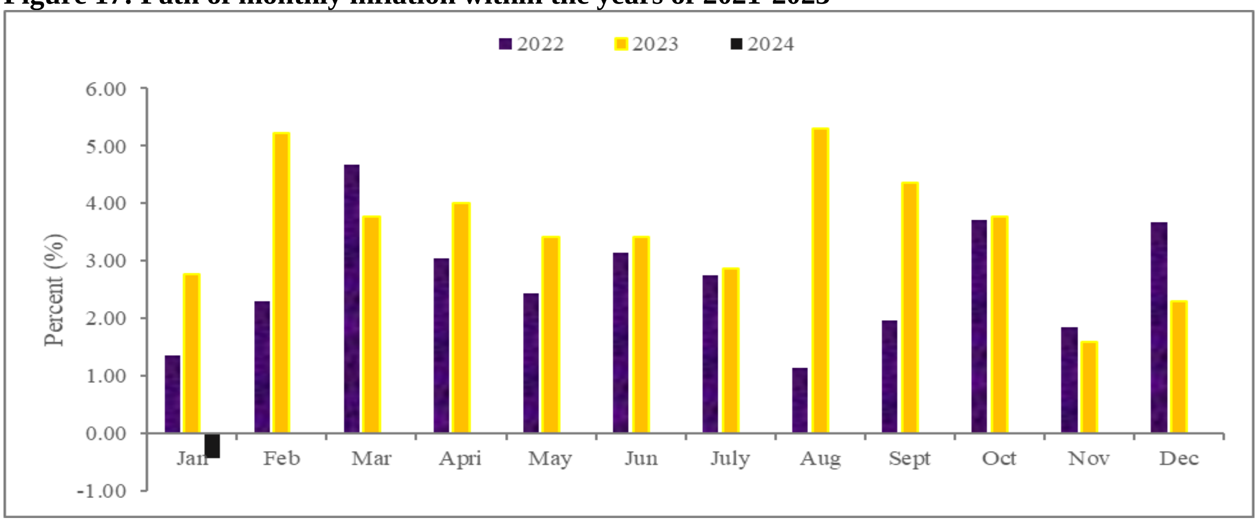
Figure 16: Headline, Food and Non-food Inflation



Source: Statistics Sierra Leone

On a month-on Month basis, inflation declined to 0.4 percent in January 2024 from 2.2 percent in December 2023. The decline in January was broad based, reflecting faster-than expected price declines associated with market-based goods and services such as food, and regulated services.

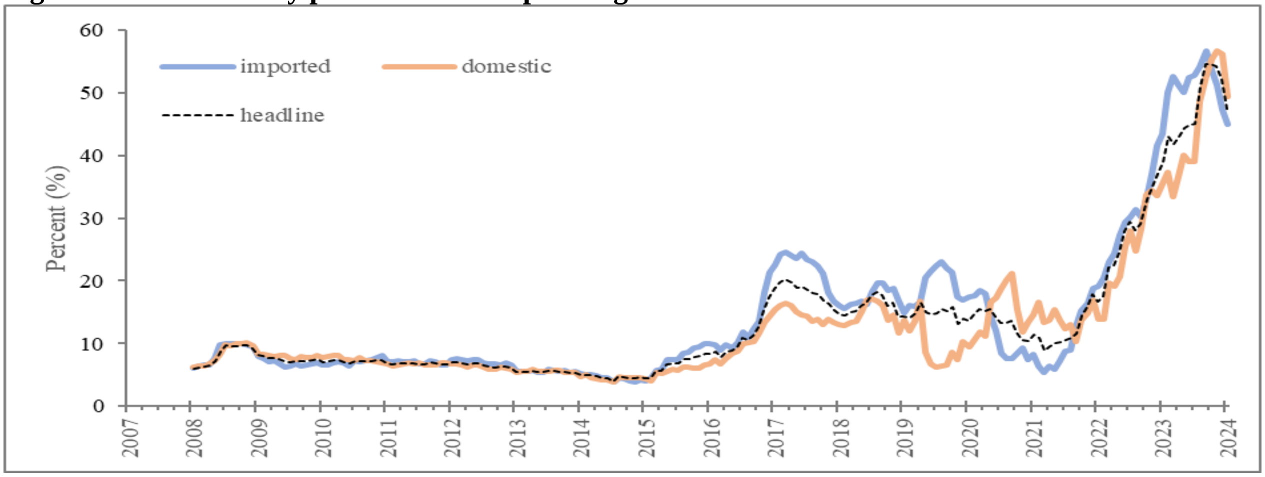
Figure 17: Path of monthly inflation within the years of 2021-2023



Source: Statistics Sierra Leone

Broad assessment of inflation showed that both imported and domestic goods and services inflation subsided in the 2023Q4 and January 2024. This implies that domestic inflationary pressures as well as imported inflation eased in the review period.

Figure 18: Domestically produced and imported goods and services inflation



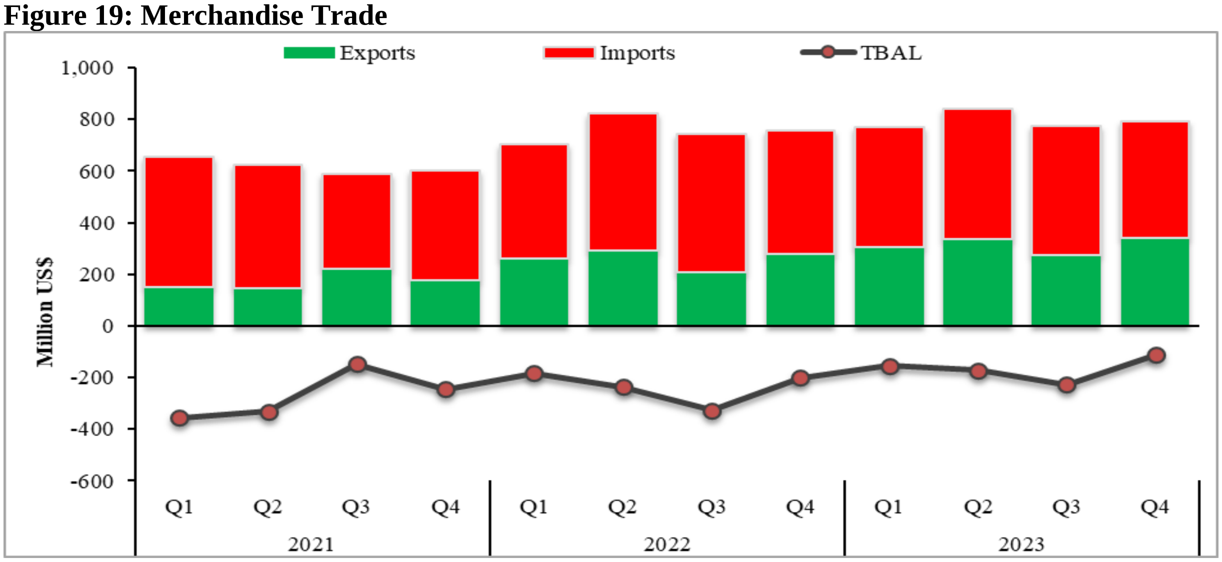
Source: Statistics Sierra Leone and BSL

2.2 External Sector Developments

2.2.1 Merchandise Trade

Sierra Leone's trade deficit with the rest of the world narrowed by 50.89 percent to US$111.30mn in 2023Q4 from US$226.62mn in the previous quarter, reflecting the combined effects of a 24.26 percent increase in exports receipts, coupled with a 9.72 percent decrease in import bills.

Figure 19: Merchandise Trade



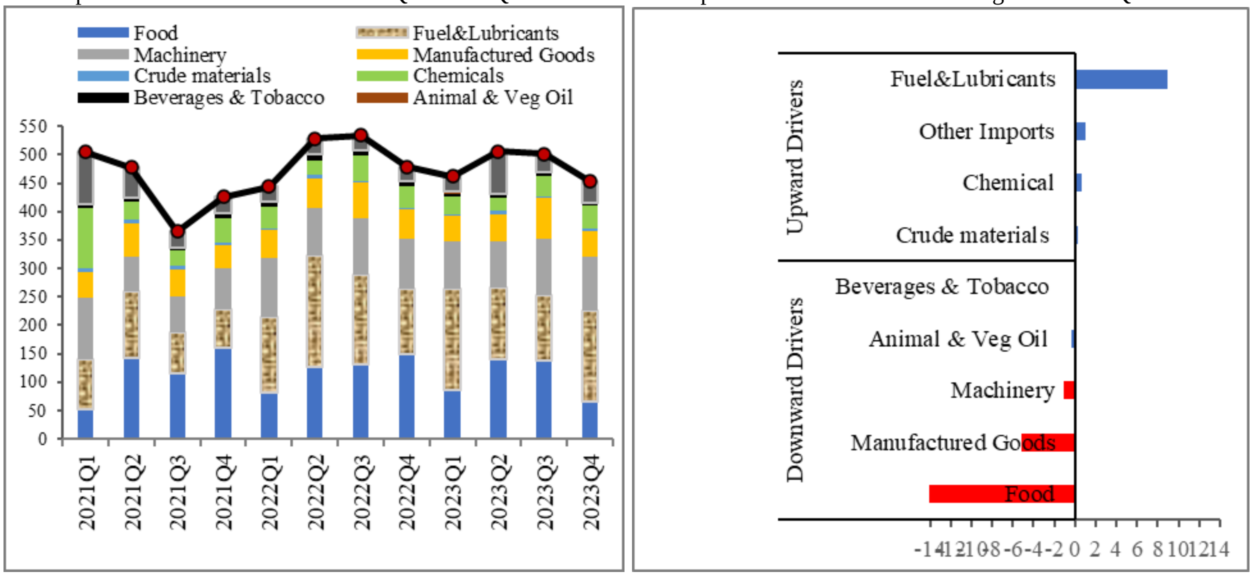
Source: NRA/Customs & BSL

Components of Import

Merchandise imports were driven down by food and manufactured goods, which was only partially offset by the boost from fuels and lubricants. Merchandise imports were valued at US$452.5mn in 2023Q4, decreasing by 9.7 percent from 2023Q3.

Figure 20: Components of Import

A: Imports-relative contributions 2020Q1 – 2023Q3 B: Imports-relative contributions to growth 2023Q3



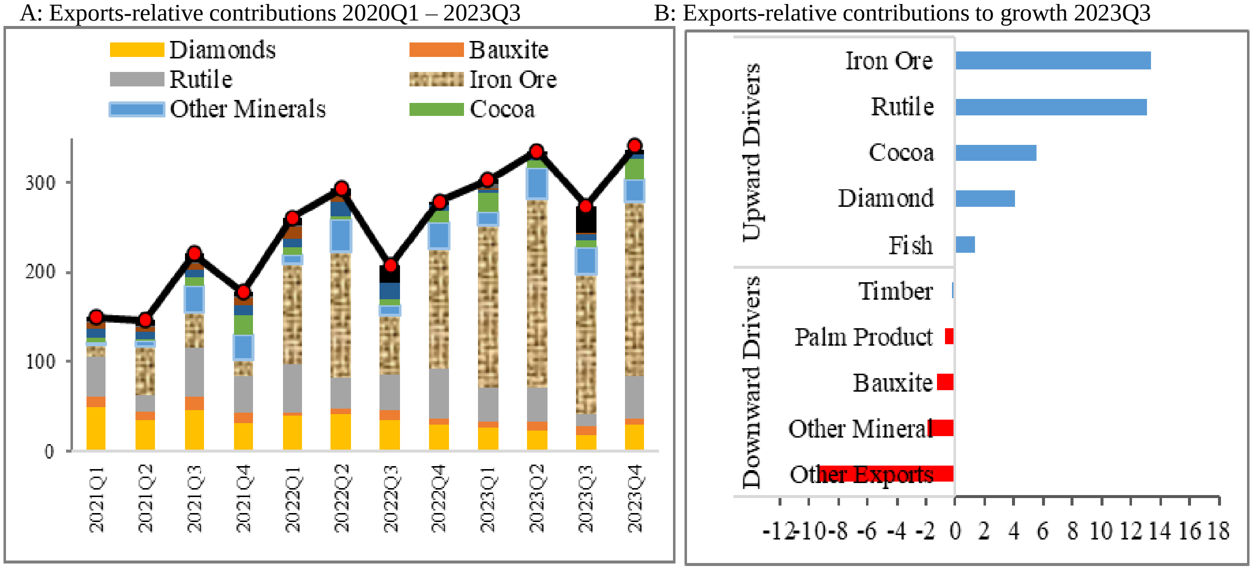
***Source**: NRA/Customs & BSL*

Components of Export

The increase in merchandise exports was driven mainly by iron ore, rutile, cocoa, and diamonds, which was only in small part offset by other exports. Total value of merchandise exports increased by 24.3 percent from 2023Q3 to US$341.2mn in 2023Q4.

Figure 21: Components of Export

A: Exports-relative contributions 2020Q1 – 2023Q3 B: Exports-relative contributions to growth 2023Q3

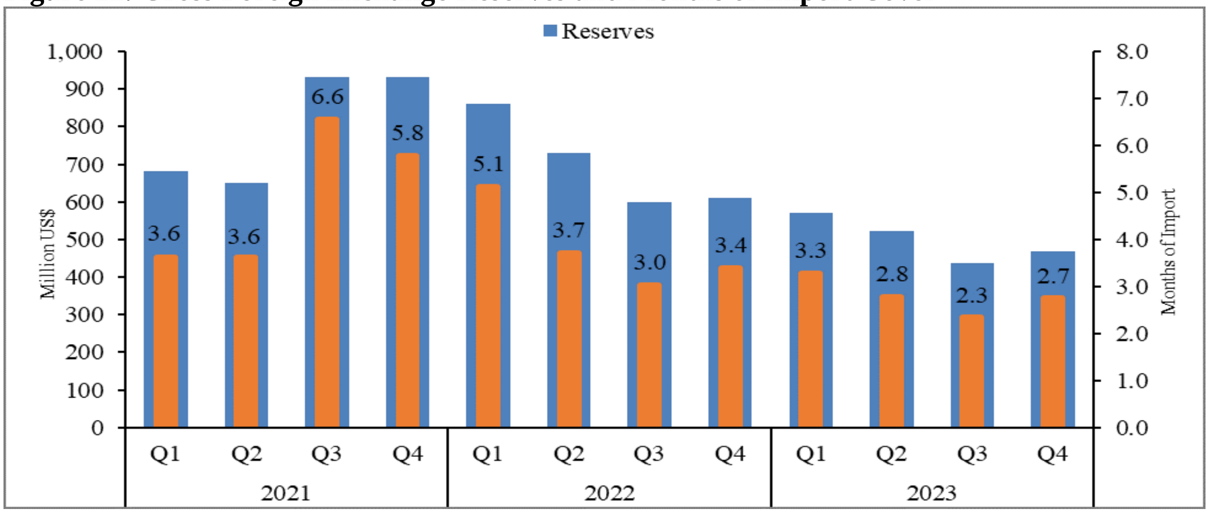


***Source**: NRA/Customs & BSL*

2.2.2 Gross Foreign Exchange Reserves

Gross foreign exchange reserves of the Bank of Sierra Leone increased to US$468.4mn in 2023Q4 from US$437.5 million in 2023Q3, mainly on account of excess inflows over outflows during the review quarter. Consequently, reserves were enough to cover 2.7 months of import of goods and services in 2023Q4, compared with 2.3 months of import cover in 2023Q3.

Figure 22: Gross Foreign Exchange Reserves and Months of Import Cover

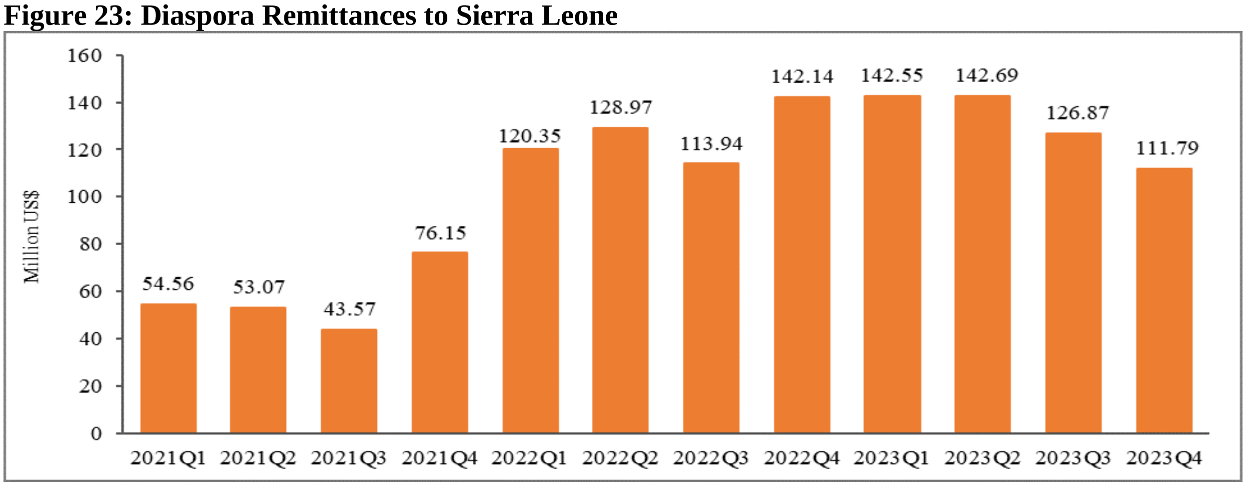


Source: Bank of Sierra Leone (BSL)

2.2.3 Diaspora Remittances

Diaspora remittance inflows further decreased by 11.9 percent to US$111.8mn in 2023Q4, from US$126.9mn in 2023Q3. Remittances are however expected to be stronger in the next quarter, as Sierra Leoneans in the diaspora support families and friends back home.

Figure 23: Diaspora Remittances to Sierra Leone

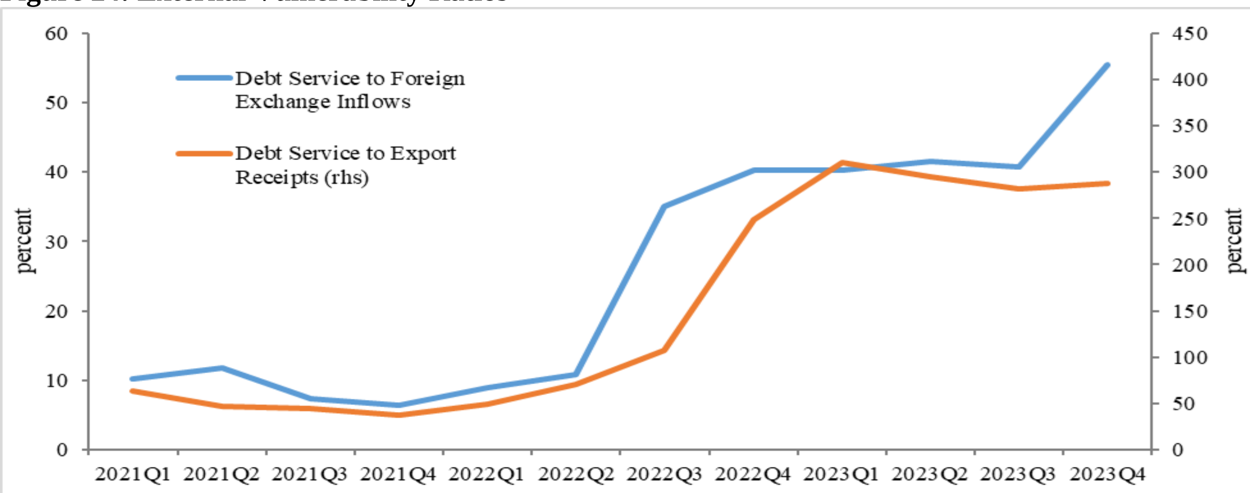


Source: Bank of Sierra Leone (BSL)

2.2.4 External Vulnerability Ratios

External debt service payments increased to US$53.9mn in 2023Q4, from US$27.2mn in 2023Q3. Similarly, forex inflows and export tax receipts also increased to US$117.67mn and US$12.28mn in 2023Q4 from US$18.44mn and US$9.30mn, respectively, in 2023Q3. Accordingly, the ratio of debt service to export tax receipt was broadly stable in 2023Q4, while that of debt service to FX inflows increased.

Figure 24: External Vulnerability Ratios



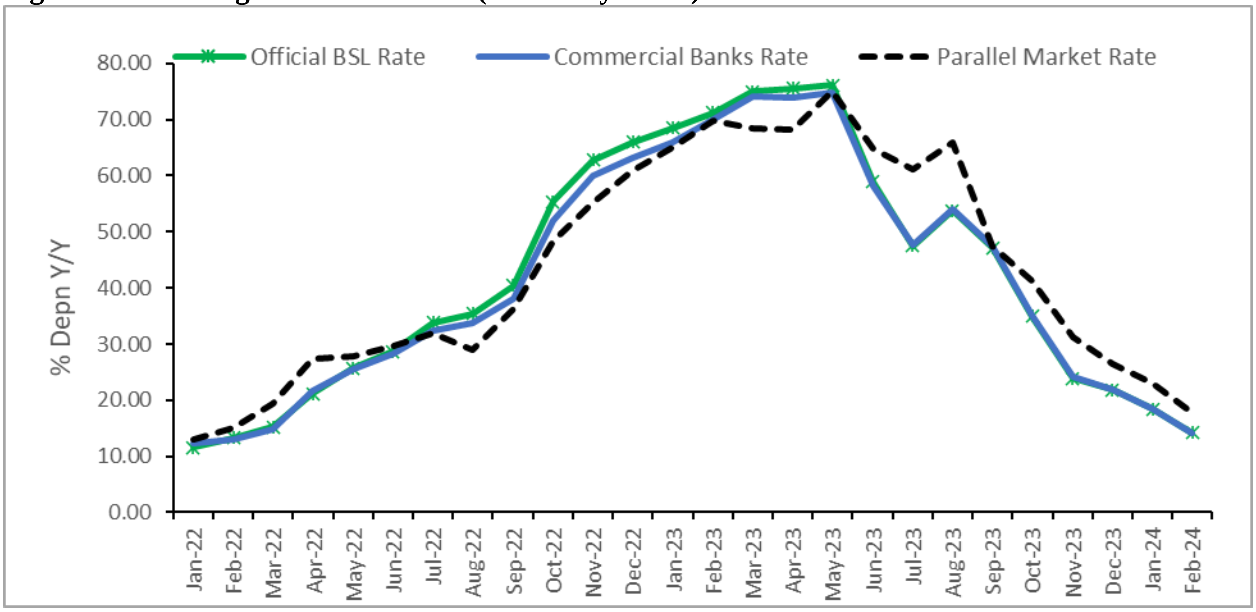
Note: Debt service ratios are calculated using the 4-quarter sums of the relevant variables, thereby smoothing the series.
Source: Bank of Sierra Leone (BSL)

2.3 Exchange Rates and Foreign Exchange Market Developments

2.3.1 Bilateral Rates and Foreign Exchange Market Developments

The exchange rate has been relatively stable since July 2023 owing to tighter monetary policy, some other policy measures (such as prohibiting offshore trading by international brokerage firms and repatriation of export proceeds as stipulated in Finance Act 2024) implemented by BSL and supported by tighter fiscal policy. These measures also contributed to improving foreign trade balance, which in turn reduced pressure on the foreign exchange market. Furthermore, with the stabilization of the exchange rate, speculation in the FX market also subsided in 2023Q4 to January 2024 thereby leading to reduced hedging activities by market participants and lower volatility.

Figure 25: Exchange Rate Movement (Year-on-year %)



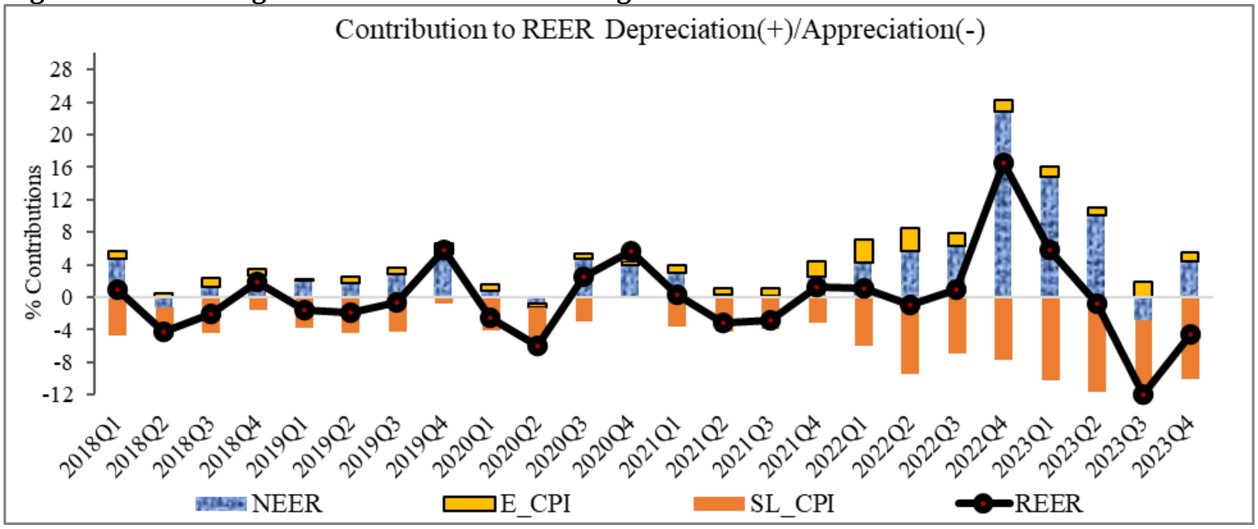
Source: Bank of Sierra Leone (BSL)

2.3.2 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 appreciated by 4 percent in 2023Q4, relative to 2023Q3.

Similarly, the real effective exchange rate (REER), which measures the competitiveness of SierraLeone's traded goods relative to those of its trading partners appreciated by 5 percent in 2023Q4 relative to 2023Q3. The REER appreciation was due to a significant increase in domestic prices compared to foreign prices, which outweighed the effect of nominal depreciation.

Figure 26: Percentage Contributions to the Change in REER



Note: positive NEER and REER denote depreciation and negative means appreciation
Source: BSL, staff estimation.

Figure 27: Real Effective Exchange Rate

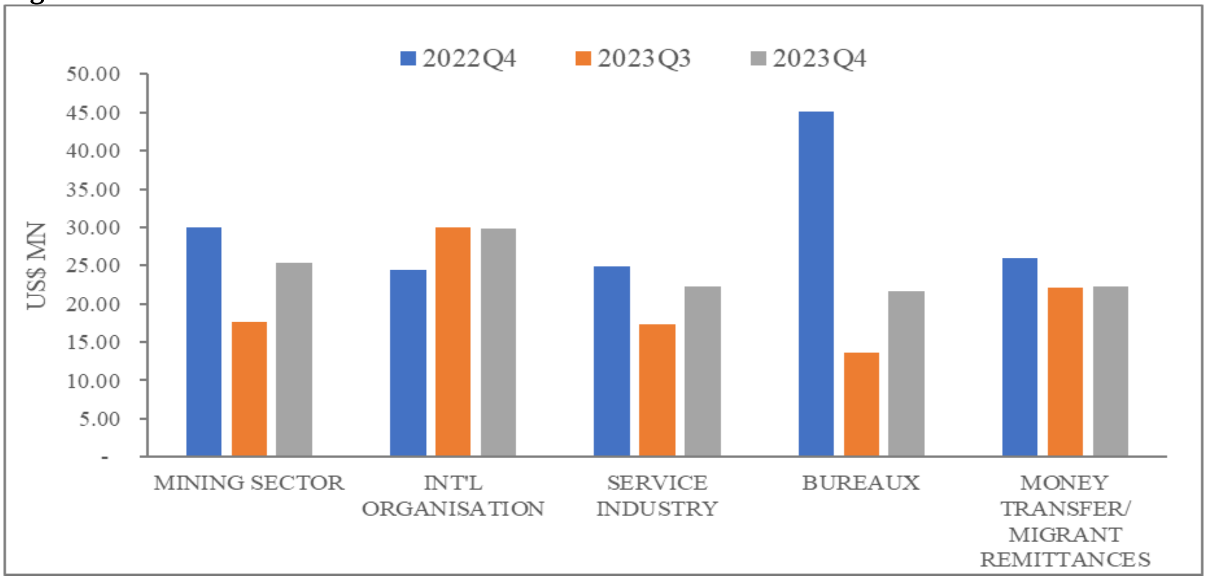
Source: BSL, staff estimation

2.3.3 Foreign Exchange Market Turnover

Total amount traded in the foreign exchange market (purchases and sales) during 2023Q4 was US$332.40mn, down by 16.1 percent relative to US$396.23mn realized in the corresponding quarter (2022Q4) and up by 9.7 percent from US$303.12mn recorded in 2023Q3.

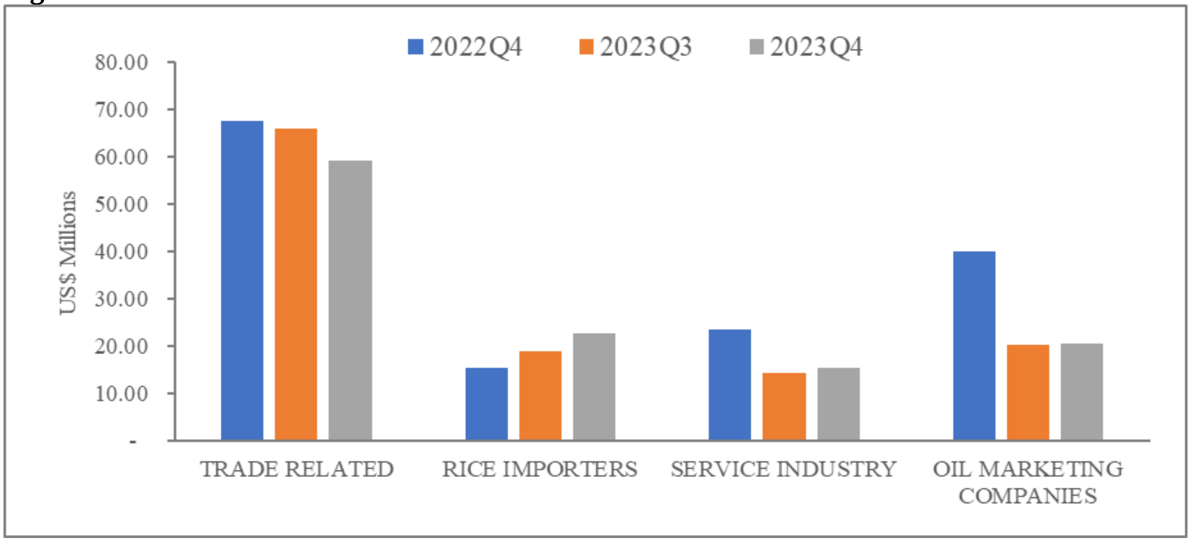
Commercial banks mainly purchase forex from the mining sector, international organizations (mostly NGO's), foreign exchange bureaus, and the service industry. Foreign exchange from remittances is typically acquired either from remittance companies or indirectly from FX bureaus. Banks traditionally provide foreign exchange to various entities, such as rice importers, oil marketing companies, and businesses in the service industry.

Figure 28: Commercial Banks' Forex Purchases from Selected Sectors



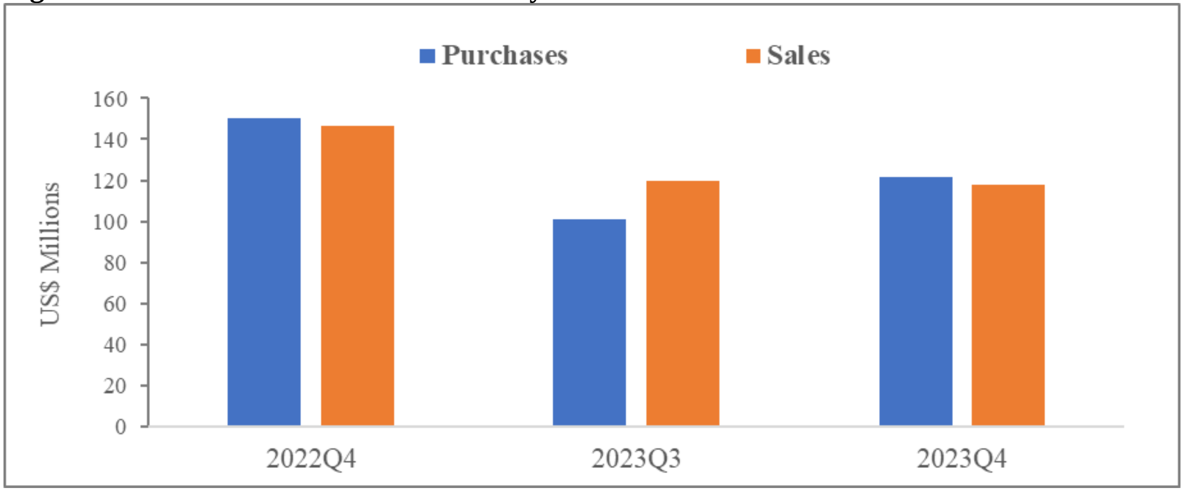
Source: Bank of Sierra Leone (BSL)

Figure 29: Commercial Banks Forex Sales to Selected Sectors



Source: Bank of Sierra Leone (BSL)

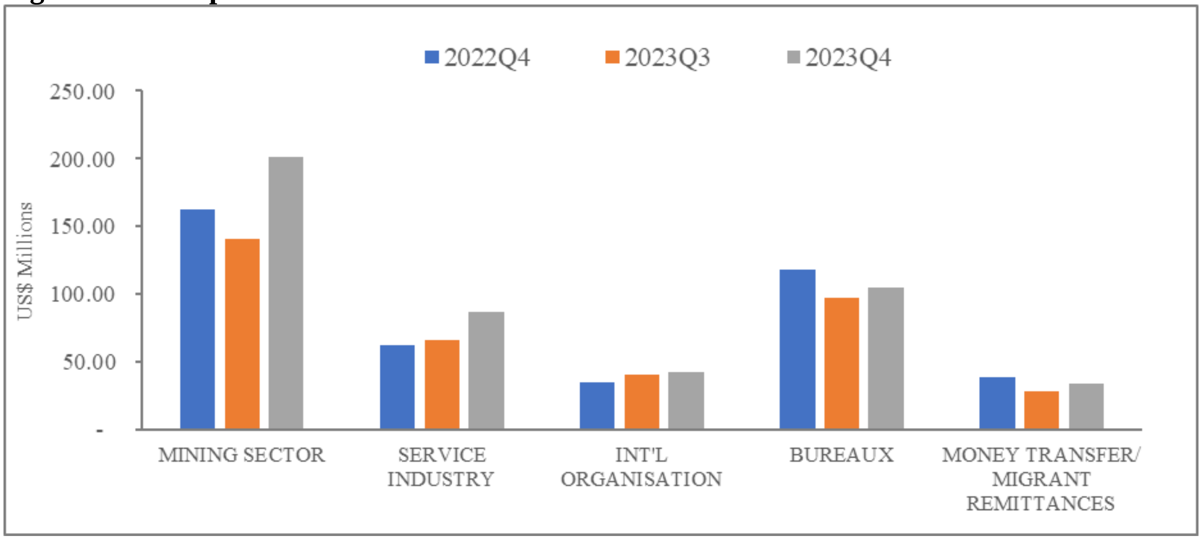
Figure 30: Purchases and Sales of Forex by Commercial Banks



Source: Bank of Sierra Leone (BSL)

Receipts into customer foreign currency accounts increased in 2023Q4 by 12.3 percent to US$601.78mn from US$535.88mn recorded in the corresponding period in 2022. The major contributors for the increase in receipts were from the mining sector, service industry, and international organization/NGO. On the other hand, receipts into customer foreign currency accounts also increased by 21.3 percent from US$496.08mn in 2023Q3 to US$601.78mn in 2023Q4 on account of increase from the mining sector, service industry, international organization/NGO's, forex bureaus, and migrant remittances.

Figure 31: Receipts into CFC Accounts – Selected Sectors



Source: Bank of Sierra Leone (BSL)

2.3.4 Outlook to the Foreign Exchange Market

The exchange rate is expected to remain stable in 2024Q1 as tighter monetary and fiscal policies continue to reduce the pressure on the exchange rate, which is assessed to be close to equilibrium value. Furthermore, supply of forex is expected to increase on account of the enforcement of the minimum 30 percent export repatriation proceeds policy as enshrined in the Finance Act of 2024.

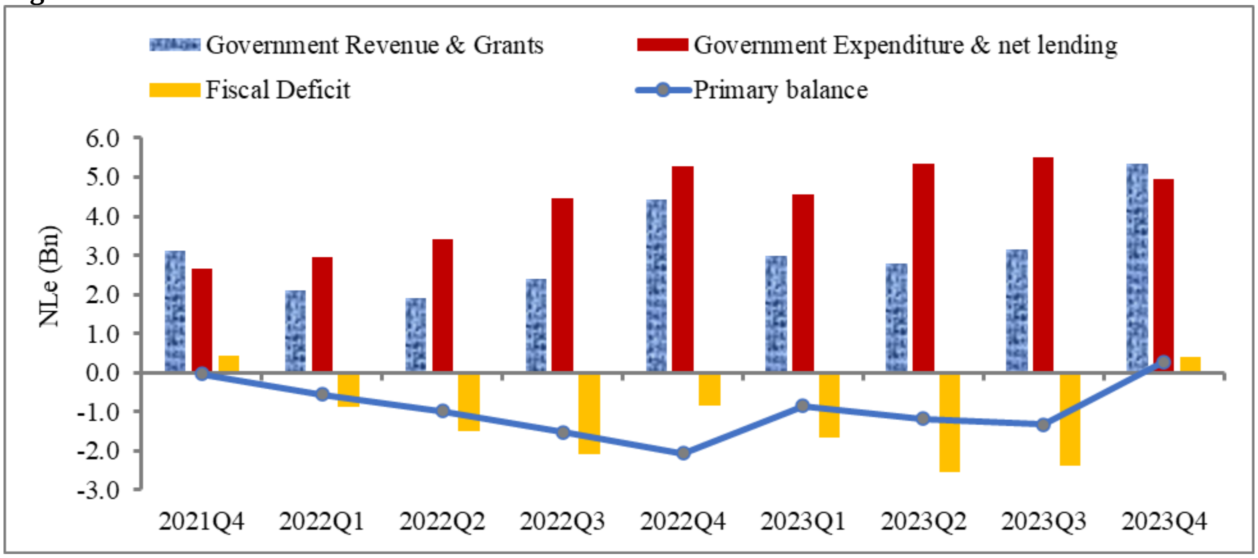
2.4 Fiscal Development

2.4.1 Fiscal Policy Stance

Overall government budgetary performance improved in 2023Q4. Hence, government budgetary operations recorded a surplus of NLe0.4bn compared to a deficit of NLe2.4bn in 2023Q3 and NLe2.6bn in 2023Q2. The improvement in fiscal outturn reflected largely the expansion in foreign grants coupled with increased revenue collection and a contraction in expenditure. Accordingly, primary balance recorded a surplus of NLe0.3bn in 2023Q4, compared to a primary deficit of NLe1.3bn in 2023Q3.

On a yearly basis, preliminary assessments of government fiscal performance suggest that fiscal deficit narrowed to a deficit of 8.4 percent of GDP in 2023 compared to 9.4 percent of GDP in 2022, yet higher than the ECF program target of 5.8 percent of GDP. This decline in the deficit can be attributed to reduction in expenditures. The overall deficit is expected to further improve in the medium term, explained by improved domestic revenue mobilization and expenditure rationalization. Likewise, the primary deficit narrowed to 3.9 percent of GDP in 2023 compared to 9.0 percent of GDP in 2022.

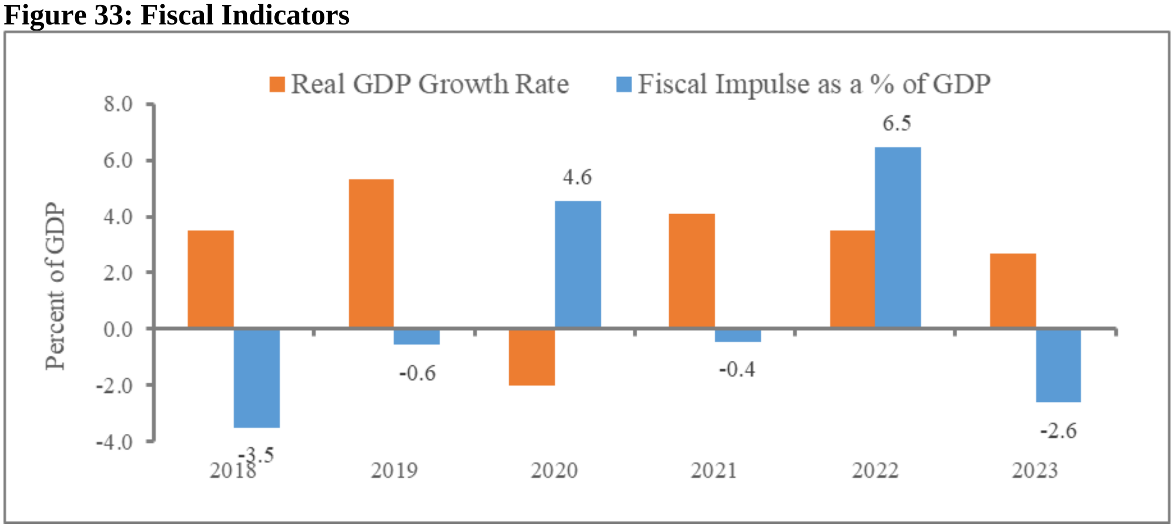
Figure 32: Fiscal deficit



Source: Ministry of Finance (MoF)

The preliminary fiscal stance was contractionary in 2023 compared to 2022. The narrowing of the domestic primary deficit exerted negative fiscal impulse on domestic demand. The lower deficit was consistent with the improvement in domestic revenue mobilization combined with a reduction in discretionary expenditure (the ongoing tight fiscal measures such as removal of subsidies and transfers, and the introduction of new taxes). Consequently, these fiscal measures could constrain consumer spending and hence subdue aggregate demand and inflation.

Figure 33: Fiscal Indicators



Sources: Ministry of Finance (MoF) & Bank of Sierra Leone (BSL)

2.4.2 Government Revenues and Grants

On a quarterly basis, total revenue and grants recorded 6.9 percent of GDP (NLe5.3bn) in 2023Q4 reflecting an increase of 3.5 percentage points compared to 3.3 percent of GDP (NLe3.2bn) in the preceding quarter. This amount exceeded the quarterly target of NLe3.9bn by 35.9 percent. The overperformance in total revenue stemmed largely from larger foreign grants and higher domestic revenue.

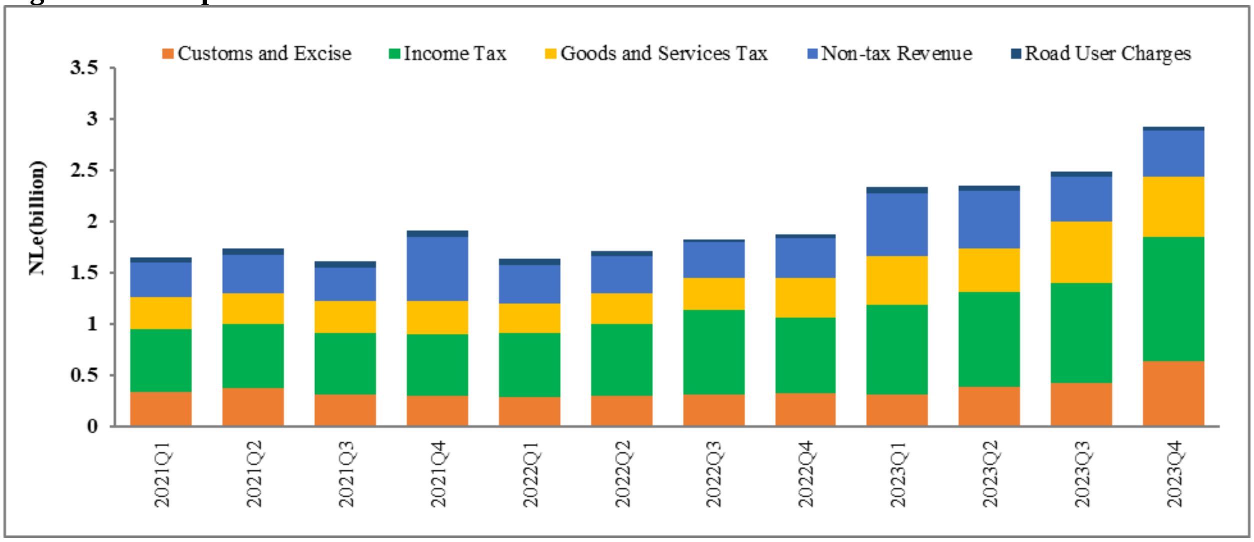
Domestic revenue rose to NLe2.9bn in 2023Q4 (3.7 percent of GDP), from NLe2.5bn in 2023Q3, yet it was 7.9 percent lower than the target of NLe3.9bn. The increase in revenue can be mainly attributed to the increase in corporate and personal income taxes due to the introduction of a turnover Minimum Alternate Tax (MAT), excise duties on petroleum products, import dutiesand other excise taxes. The rise in excise duties could be explained by the convert ad-valorem excise duty to specific products and the harmonization of excise rates on domestic goods and imports among other taxes implemented combined with strengthening of tax compliance. However, the goods and services tax (GST) declined nominally despite high inflation. Overall, tax revenue was 3.1 percent of GDP (NLe2.44bn) in 2023Q4, above the previous quarter's 2.7 percent of GDP (NLe2.0bn), and it exceeded the target (NLe2.41bn) marginally, by 1.2 percent.

Non-tax revenue also increased marginally by 1.8 percent (NLe0.44bn) but fell short of the quarterly target by 38.7 percent (NLe0.71bn). Revenue from TSA collected from other departments and petroleum licenses contributed to the slight increase in non-tax revenue. On the other hand, receipts from road user charges and vehicle licenses fell to NLe0.42bn in 2023Q4 from NLe0.46bn in 2023Q3.

Total foreign grants received amounted to NLe2.4bn in 2023Q4 (3.1 percent of GDP) representing a significant increase of 261.5 percent compared to NLe0.7bn in 2023Q3 and was higher than the quarterly target of NLe0.8bn. This amount comprised of budgetary support disbursed by the World Bank amounting to NLe1.5bn and a project grant amounting to NLe0.9bn. Foreign grants exhibit a seasonal pattern as they show a big spike in the fourth quarter.

Total revenue and grants (on a year-on-year basis) moderated to 18.1 percent of GDP in 2023 compared to 18.9 percent in 2022 owing to a decline in foreign grants received, while domestic revenue collected improved. However, total revenue and grants is projected to expand averaging 20.7 percent of GDP in 2024 as a result of the implementation of Finance Act 2024.

Figure 34: Components of Domestic Revenue

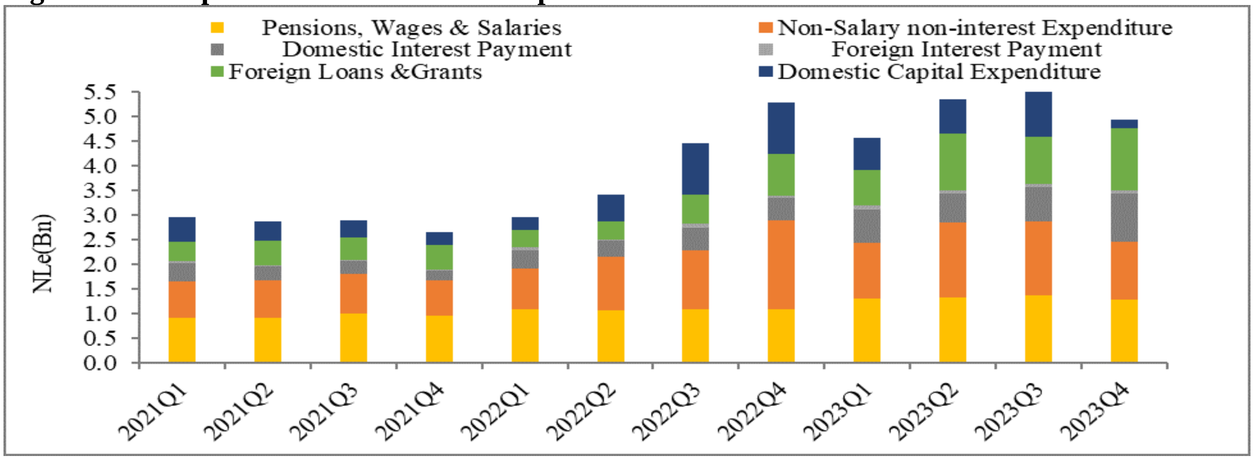


Source: Bank of Sierra Leone (BSL)

2.4.3 Government Expenditures

Total government expenditure and net lending reduced from 28.5 percent of GDP in 2022 to 25.7 percent of GDP in 2023. Similarly, on a quarter-on-quarter basis, expenditure moderated from 7.3 percent of GDP (NLe5.5bn) in 2023Q3 to 6.1 percent of GDP (NLe4.9bn) in 2023Q4, but nonetheless higher than the quarterly ceiling of NLe4.5bn. The moderation in total expenditure was mostly on account of a cut in capital spending by 0.64 percent of GDP and a decrease in recurrent expenditure by 0.54 percent of GDP. This reflects the government's drastic reduction of subsidies and domestic capital expenditure in line with the Finance Act 2023.

Figure 35: Components of Government Expenditure



Source: Bank of Sierra Leone (BSL)

Recurrent expenditure moderated to 4.5 percent of GDP (NLe3.5bn) in 2023Q4 from NLe3.6bn in 2023Q3 but breached the quarterly target of NLe3.4bn. The moderation in recurrent expenditure was largely due to the decrease in non-salary, non-interest expenditures by 0.6 percent of GDP and wages and salaries by 0.1 percent of GDP. Debt service payments increased by 0.3 percent of GDP reflecting the expansion in domestic debt service payments. The cut in non-salary,non-interest spending stemmed from a significant reduction in subsidies and transfers and decline in goods and services spending.

Capital expenditure contracted by 0.7 percent of GDP (NLe1.4bn) in 2023Q4, from NLe1.9bn in 2023Q3, yet significantly exceeded the quarterly ceiling of NLe1.0bn. The drop in capital expenditure was due to a decline in domestic capital expenditure. However, foreign financed capital expenditure increased during the review quarter.

2.4.4 Outlook to the fiscal sector

The overall deficit is expected to moderate further in 2024 and over the medium term (up to 2027). The consolidation efforts by the fiscal authorities were to reconstitute buffers, limit public finance risks, debt sustainability, and to complement BSL's efforts to contain inflation. Revenue is expected to expand as the governmentintensifies efforts to automate taxes, improve tax capacity and coverage highlighted in the Finance Acts. On expenditure, prioritizing target spending, enhancing spending efficiency, strengthening payroll management, lengthening debt maturities, stability of the exchange rate, and moderation in inflation could mute risks to budget execution (budget deficits dipping) and restore macroeconomic stability.

2.5 Money Markets Developments and Monetary Aggregates

2.5.1 Interest Rates Development

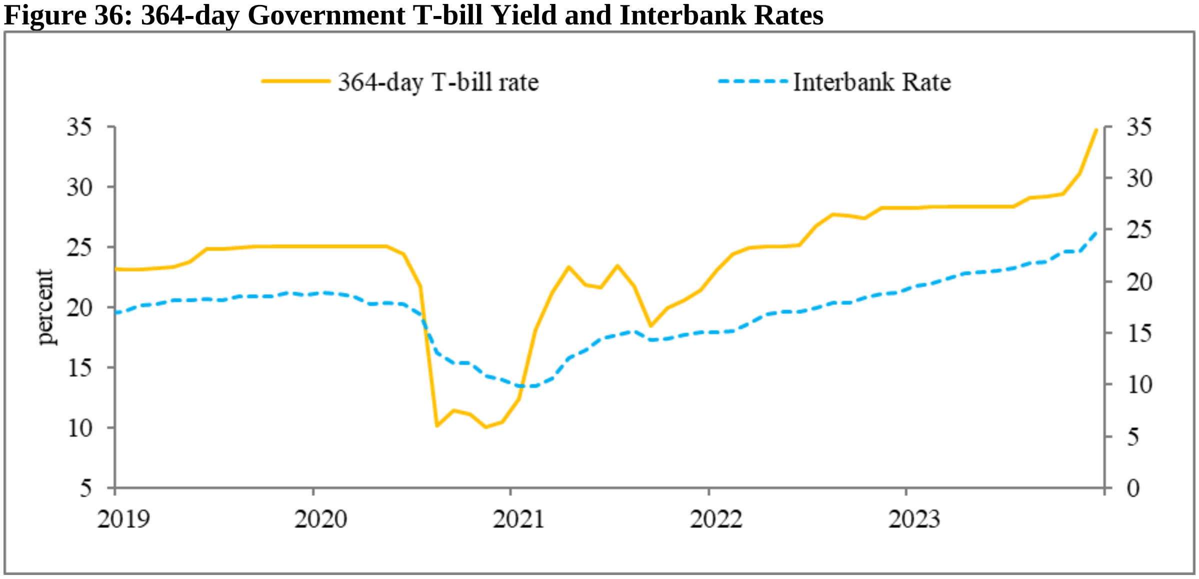
Treasury Bill Rates

The interest rate on the 364-day treasury bills increased from 29.1 percent in September 2023 to 34.7 percent in December 2023 and then further to 39.5 percent in February 2024. Meanwhile, the182-day and 91-day treasury bill markets remained highly illiquid, with their yields not reflecting the underlying economic and financial environment.

***Interbank* Money Market**

The interbank weighted average interest rate increased from 21.9 percent in September 2023 to 24.8 percent in December 2023, moving closer to the overnight standing lending rate, an indication of tight liquidity in the interbank market. The average lending rate of commercial banks decreased from 20.5percent in September 2023 to 20.2 percent in December 2023. The saving rate of commercial banks increased from 2.2 percent in September 2023 to 2.3 percent in December 2023. Consequently, the spread between the average lending rate and saving rate of commercial banks declined from 18.2 percent at end September 2023 to 17.8 percent as at end December 2023.

Figure 36: 364-day Government T-bill Yield and Interbank Rates

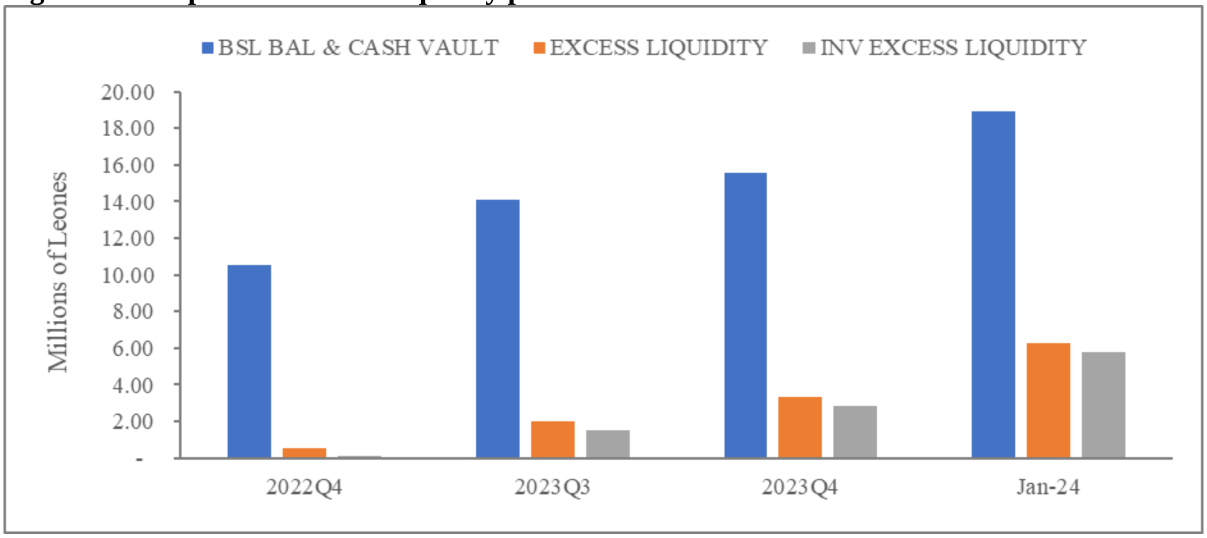


Source: Bank of Sierra Leone (BSL)

2.5.2 Liquidity in the Banking System

Total liquidity in the banking system increased by NLe0.15bn to NLe1,56bn as at end 2023Q4 from NLe1,4bn as at end 2023Q3, reflecting increase in cash-in-vault by commercial banks. The observed increase in excess liquidity as at end 2023Q4 could be explained by increased deposits with DMBs, as well as BSL intervention in the secondary market.

Figure 37: Snapshot of DMBs Liquidity position.



Source: Bank of Sierra Leone (BSL)

There was a significant decrease in the level of intermediation in the interbank money market during the review period. The volume of interbank transactions decreased by NLe2.3bn toNLe0.8bn in Q4 2023. In January 2024, the volume of transactions reached NLe0.8bn, the same volume in one month than during the entire previous quarter. No bank accessed the standing deposit facility (SDF) window, while access to the BSL standing lending facility (SLF) remained high, reflecting tight liquidity condition in the money market. However, the volume of transactions in this window by banks decreased by NLe1,9bn to NLe28,1bn in Q4 2023.

2.6 Monetary Aggregates

Both reserve money (RM) and broad money (M2) growth increased during the fourth quarter of 2023.

Reserve Money (RM)

Reserve money (RM) expanded by 20.4 percent in 2023Q4, from a contraction of 1.3 percent in 2023Q3. The expansion in RM emanated mainly from the 5.2 percent increase in the Net DomesticAssets (NDA) of the BSL which outweighed the 18.2 percent contraction in the net foreign assets(NFA) of the BSL. The growth in the NDA of the BSL was due to the 27.1 percent increase in their holdings of government securities.

On the liability side, the growth in RM was attributed to the 19.1 percent growth of currency issued, coupled with the 26.6 percent increase in commercial banks’ reserves deposited at the central bank during the same review period.

Broad Money (M2)

Broad Money expanded by 10.0 percent in 2023Q4, compared to the 8.8 percent increase recorded in 2023Q3. The growth in M2 was primarily as a result of the expansion in the Net Foreign Assets (NFA) of the banking system, which more than outweighed the contraction in the Net Domestic Assets (NDA) of the banking system.

The expansion of the NFA of the banking system was driven by build-up in the foreign currency holdings of commercial banks, while the NFA of the BSL contracted. The NDA of the banking system contracted by 0.6 percent in 2023Q4, on account of a 0.5 percent decrease in net claims on government. Net claims on government by the BSL and commercial banks contracted by 0.4 percent and 0.7 percent in 2023Q4, respectively. Credit to the private sector by commercial banks expanded by 7.4 percent in 2023Q4.

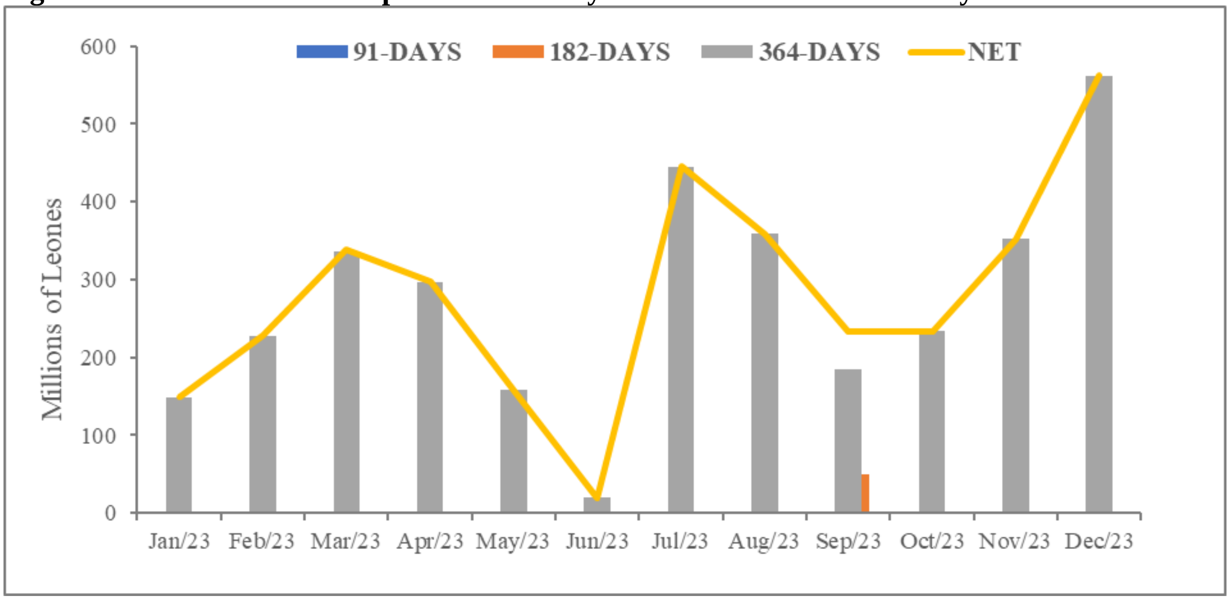
From the liability side, M2 expanded as a reflection of increase in both narrow money (M1) and quasi money. M1 expanded by 9.7 percent in 2023Q4, mainly attributed to the 16.1 percent surge in currency outside banks, while demand deposits increased by 3.6 percent. Quasi money expanded by 10.3 percent, mainly due to increases in both foreign currency deposits (13.0 percent) and time and saving deposits (4.3 percent).

On a year-on-year basis, growth in M2 moderated to 32.8 percent in 2023Q4 compared to the 41.7 percent increase recorded in 2022Q4. The annual slowdown in M2 growth was driven by both NFA and NDA of the banking system. The annual increase in M2 was above the IMF/ ECF program target of 27.2 percent as at end December 2023, but M2 was still trending down broadly in line with program requirements. On an annual basis, credit to the private sector by commercial banks expanded by 25.0 percent, which was above the IMF/ ECF program target of 18.4 percent as at end December 2023.

2.7 Domestic Debt Market

The primary market auctions for Government Securities were largely oversubscribed on a net basis during the review period. The 364-days tenure was oversubscribed for the months of January to May 2023, but was undersubscribed for the month of June 2023, whilst the 182-days and the 91- days tenures were undersubscribed throughout the year. In that regard, the demand for government treasury bills continued to be skewed towards the 364-day tenure, with deposit money banks being the primary participants. The 91 and 182-day T-bill auctions remained dysfunctional.

Figure 38: Under/Oversubscription of Treasury Bills Auctions in the Primary Market



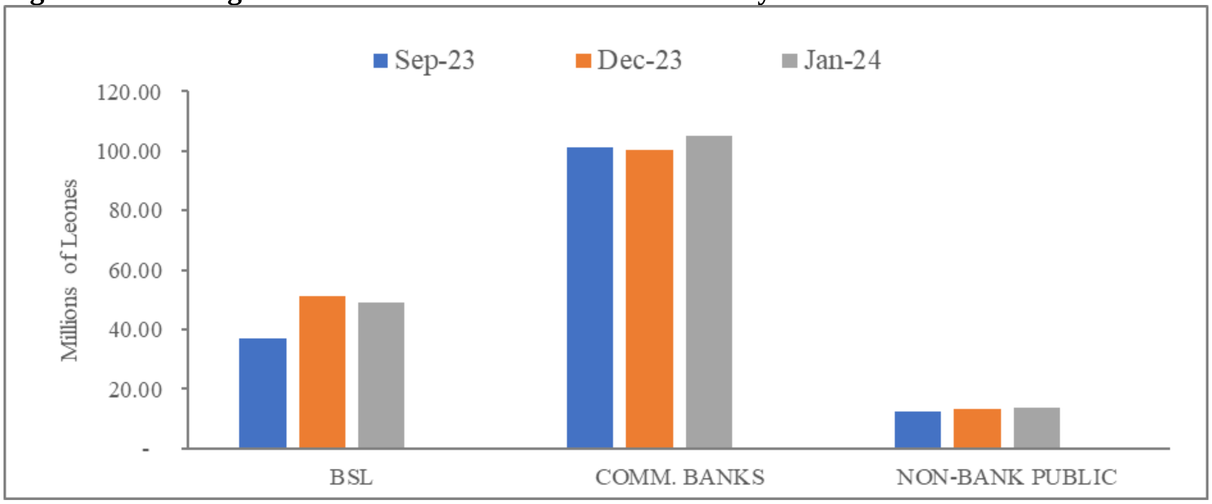
Source: Bank of Sierra Leone (BSL)

The total stock of Government securities increased by NLe1,544mn (9.1 percent) to NLe18,469mn as at end 2023Q4, relative to 2023Q3. It further increased by NLe227mn (1.2 percent) to NLe18,696mn as at end-January 2024. Marketable securities accounted for 89.3 percent of the total stock of government securities whilst non-marketable securities accounted for 10.7 percent.

The stock of marketable securities increased by NLe1,415mn (9.4 percent) from NLe15,080mn as at end 2023Q3, to NLe16,495mn as at end 2023Q4. Also, the stock further increased by Le264.5mn (1.6 percent) to NLe16,760mn as at end January 2024. The issuance of new treasury securities during the review period was mainly to finance the budget. The stock of non-marketable securities increased by NLe129mn (7.0 percent) from NLe1,845mn as at end 2023Q3 to NLe1,974mn as at end 2023Q4, on account of new issuance of 3-year Treasury bonds. However, the stock of non-marketable securities decreased by Le38mn (1.9 percent) to NLe1,936mn as at end January 2024.

As at end-December 2023, the proportion of 91-day, 182-day and 364-day treasury bills to the total marketable securities was 0.0 percent, 0.3 percent, and 90.7 percent respectively, whilst that of the 1-year and 2-year Treasury bonds were 0.2 percent and 8.8 percent, respectively. With regards non-marketable securities, the 3-year, 5- year and 10-year treasury bonds accounted for 81.2 percent, 18.6 percent and 0.2 percent, respectively.

Figure 39: Holdings of Marketable Government Securities by Sector



Source: Bank of Sierra Leone (BSL)

3. FINANCIAL STABILITY ANALYSIS

3.1 Overview of banking sector developments

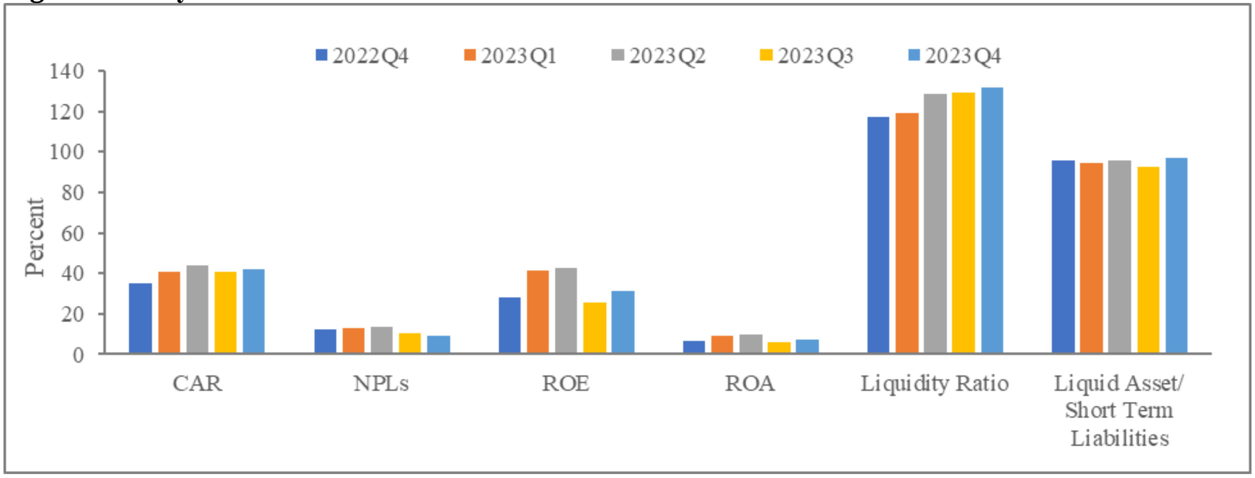
The Banking sector remained relatively stable as most of the Financial Soundness Indicators (FSIs) are within the required statutory thresholds. The stability is on account of BSL's strengthened regulatory and prudential oversight and the strong banking system profitability generated from the significant investment in government securities. Income generated from this source continued to account for the largest share of banks' total income, which reflected the positive impact on the key FSIs.

3.2 Financial Soundness Indicators (FSIs)

The banking sector continued to be stable and sufficiently capitalized. Most of the key FSIs remained within acceptable thresholds stipulated by BSL. The regulatory capital to risk-weighted asset denoted by the Capital Adequacy Ratio (CAR) increased to 41.7 percent in 2023Q4 from 40.6 percent in 2023Q3. The CAR position remained comfortably above the regulatory minimum of 15.0 percent, indicating the accumulation of sufficient capital by banks to absorb losses.

Asset quality further improved in 2023Q4 as the ratio of non-performing loans to gross loans declined to 8.8 percent in 2023Q4 from 10.6 percent in 2023Q3 and remained below the maximum limit of 10.0 percent. Banks' profitability increased in the review period as both Return on Asset (ROA) and Return on Equity (ROE) increased to 7.0 percent and 31.5 percent respectively in 2023Q4 compared to 5.7 percent and 25.5 percent respectively in 2023Q3. The Liquidity Ratio in the Banking Sector further increased in 2023Q4 to 131.9 percent relative to 129.6 percent in 2023Q3. However, liquid assets to short-term liabilities marginally declined in the review period from 53.8 percent in 2023Q3 to 53.0 percent in 2023Q4 as a result of less than proportionate increase in total liquid asset as compared to the increase in the Shareholders' fund. Loans to deposits ratio in local currency marginally improved in 2023Q4 to 38.8 percent from 36.3 percent in 2023Q3 and remained far below the regulatory threshold of 80.0 percent, indicating low level of financial intermediation by commercial banks to support economic growth.

Figure 40: Key FSI's Indicators

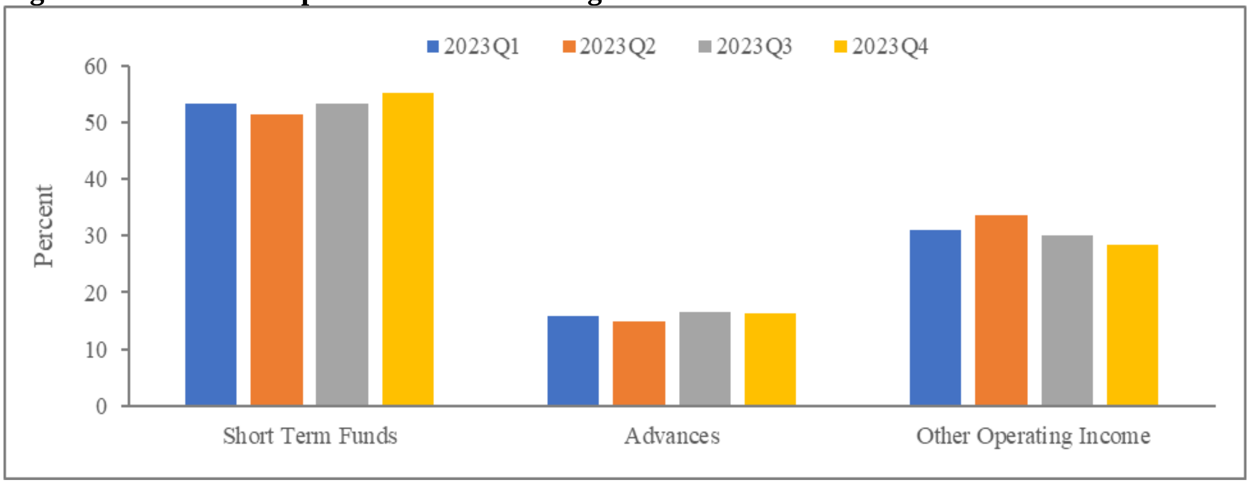


Source: Bank of Sierra Leone (BSL)

3.3 Income composition

The banking sector continued to rely primarily on government securities as its main source of income. This was mainly because rates of government securities were higher at 38.0 percent compared to average lending rate of 25.0 percent and there was zero risk on government securities investment. In 2023Q4, the proportion of income from short-term funds marginally increased from 53.4 percent in 2023Q3 to 55.3 percent in 2023Q4. On the other hand, income from loans and advances marginally decreased from 16.5 percent in 2023Q3 to 16.4 percent in 2023Q4 due to 34.1 percent increase in interest expense between the two periods. Other operating incomes, which consist mainly of commissions, fees and profits on foreign exchange dealings also decreased from 30.1 percent in 2023Q3 to 28.3 percent in 2023Q4.

Figure 41: Income Composition for the banking sector

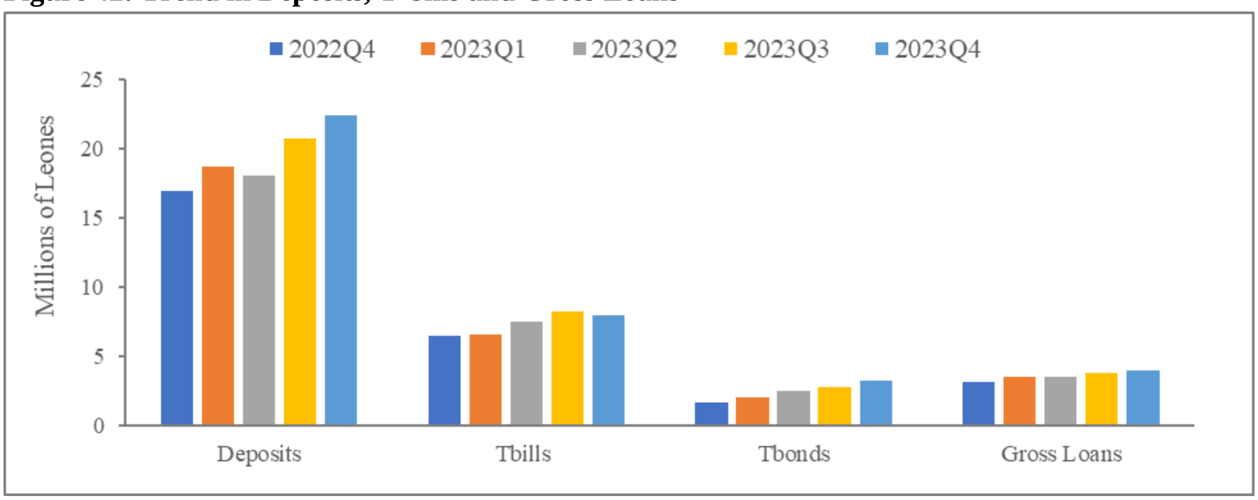


Source: Bank of Sierra Leone (BSL)

3.4 Sources and utilization of funds

- Total Deposits, which is the main source of funds for banks increased by 8.2 percent in 2023Q4 to NLe22.4 million from NLe20.7 million in 2023Q3 of which demand, savingsand time deposits accounted for 60.3 percent, 34.8 percent and 4.9 respectively in 2023Q3, and 59.0 percent, 35.9 percent, and 5.1 percent respectively in 2023Q4.
- T-bills holdings by the banking sector marginally decreased by 2.6 percent from NLe 8.2million in 2023Q3 to NLe8.0 million in 2023Q4 due to tight liquidity in the interbank markets, though interest rates increased continuously in 2023.
- T-bonds holdings by the banking sector increased by 13.9 percent from NLe2.8 millionin 2023Q3 to NLe3.2 million in 2023Q4.
- The loans to deposits ratio in local currency marginally increased in 2023Q4 to 38.8 percent from 36.6 percent in 2023Q3 and remained far below the prudential threshold of 80.0 percent, suggesting there is room for improvement.
- Gross loans and advances increased by 9.9 percent from NLe3.8 million in 2023Q3 to NLe4.0 million in 2023Q4.

Figure 42: Trend in Deposits, T-bills and Gross Loans



Source: Bank of Sierra Leone (BSL)

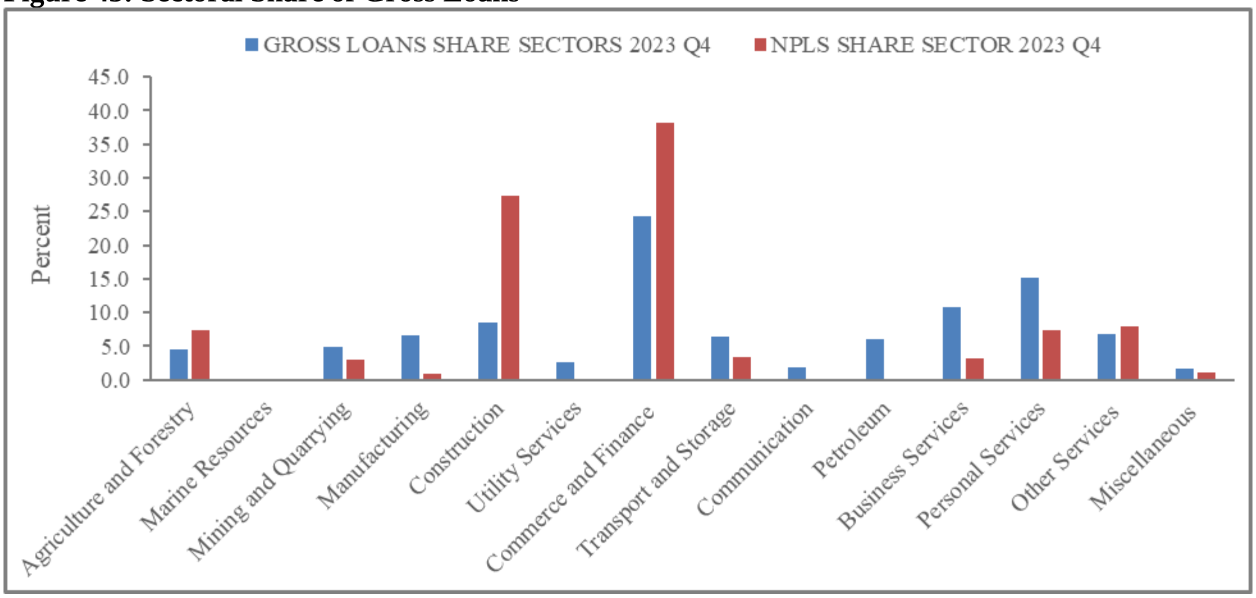
3.5 Sectoral distribution of gross loans & advances and NPLs

Commerce and Finance, Business Services, Personal Services and Construction dominated the loan portfolios of the banking sector in 2023Q4. These four sectors accounted for 58.6 percent of gross loans in 2023Q4.

Similarly, commerce and finance, construction and other services sectors contributed the most to NPLs.

In terms of sectoral NPLs, the Commerce and Finance sector had the highest NPL ratio though it only accounted for 24.2 percent of the total gross loans of the banking sector. This is partly due to supply chain disruptions and domestic macroeconomic challenges as most of the clients in that sector are importers. Fluctuations in the exchange rates could have an adverse effect on their businesses that can lead to higher costs. Construction and the Other Services sectors also had high NPL ratios of 27.3 percent and 7.9 percent respectively in 2023Q4.

Figure 43: Sectoral Share of Gross Loans

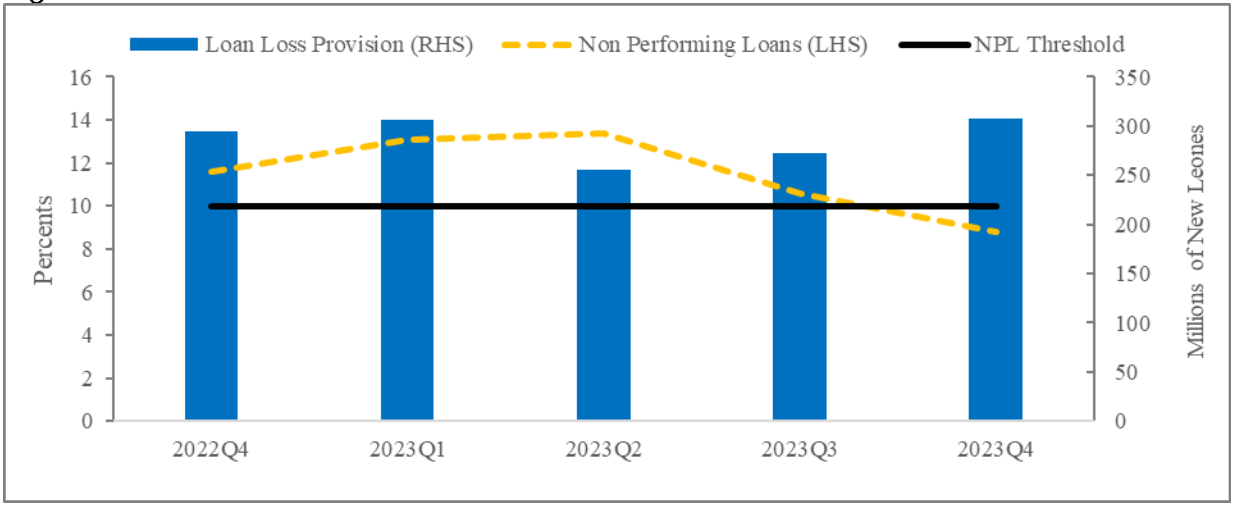


Source: Bank of Sierra Leone (BSL)

3.6 NPL Trend and Loan Loss Provisions

The proportion of Non-Performing Loans (NPLs) to gross loans fell within the review period of 2023Q4. The NPL ratio for 2023Q4 decreased by 17.6 percent from 10.6 percent in 2023Q3 to 8.8 percent in 2023Q4. However, Loan loss provisions increased by 13.1 percent to NLe307.9 million in 2023Q4 from NLe272.2 million in 2023Q3.

Figure 44:Trend of NPLs and Loan Loss Provision



Source: Bank of Sierra Leone (BSL)

3.7 Risks and Vulnerabilities to the Stability of the banking sector

Despite the stability of the financial system, there are some risks and vulnerabilities, which could pose threats to the banking sector as follows:

High levels of NPLs pose a Financial Stability Risk

Whilst the aggregate capital adequacy ratios appear strong and are comfortably above the minimum threshold with NPLs below 10.0 percent, asset quality remains a concern as thereare large variations in asset quality, with three banks recording NPLs far above the maximum threshold with two of those banks being local banks. In addition, two sectors (Commerce & Finance and Construction) are particularly vulnerable to NPLs.

Limited Intermediation to Support Economic Growth

Banks are not lending enough to the private sector partly because of the crowding out effect of investment in government securities and lending is also concentrated in a few sectors and few big customers in the economy. Out of fourteen commercial banks, there were only four banks whose lending in relation to their total deposits exceeded 25 percent (CMB, Access Bank, Skye Bank and Vista Bank).

Banking Sector Earnings are Heavily Reliant on Government Securities

Banks use customers' deposits to fund investments in government securities. Banks' excessive preference for government securities at the expense of credit to the private sector could expose them to fall in earnings in the event of a fall in interest rates and reduction in Government appetite to borrow funds in the securities market. In addition, this may be a potential source of liquidity challenges for banks.

Fraud, Cyber Security and Information Technology Threat

Potential threats to cyber security due to shift from traditional banking to more technology driven banking. There has been an increase in fraud and cybercrime cases in the banking sector.

3.8 Outlook of the banking sector

The banking sector is expected to be relatively stable going forward given that most of the banking sector assets are government securities. Increased government borrowing will continue to provide risk-free investment opportunities for banks thereby improving the risk weighted assets of the banking sector. However, continued depreciation of the local currency may reduce real profits.

Interest from investments in government securities will continue to be the main source of income for banks as long as Government appetite for funds remains elevated. However, rising inflation and depreciating Leone can reduce the fiscal space, leading to the accumulation of arrears, which can impact the NPLs of the banking sector.

Continuous stress testing process of the banking sector will enhance the supervision of systemically important banks and assess their capacity to absorb losses during stressful conditions.The completion and application of the Non-Performing Loans (NPL) strategy by Bank of Sierra Leone will help improve credit performance in the banking sector. Enhanced supervision will remain in place for four banks, including the two state-owned banks, to strengthen their capacity to handle unforeseen shocks and strengthen governance and credit administration.

4. CONCLUSION AND DECISION OF THE MPC

4.1 Conclusion

Inflationary pressures have been easing since October 2023. Headline inflation decreased from 54.6 percent in October 2023 to 52.2 percent in December 2023. Inflation further declined to 47.4 percent in January and then to 42.6 percent in February 2024 due to a broad-based decline in prices of both food and non-food items. The MPC is of the view that easing inflationary pressures reflect the tight monetary policy stance of the BSL, the relative stability of the exchange rate and moderating global commodity prices, supported by tight fiscal policy. Nonetheless, there are upside risks to the inflation outlook, including, the short-term impact of the proposed fiscal measures in the 2024 Finance Act, through direct and indirect price effects, volatility in energy prices amidst the ongoing decrease in production by the Organization of the Petroleum Exporting Countries (OPEC), and high inflation expectations.

Real GDP growth is projected to increase to 4.7 percent in 2024 and 5.2 percent in 2025, from a subdued growth of 2.7 percent in 2023. The projected expansion is to be driven by the expected increase in investment in agriculture, mining activities and a recovery in the services sector. Furthermore, the Bank's Composite Index of Economic Activities (CIEA) recorded positive growth in economic activity in 2023Q4 compared to a sharp contraction in 2023Q3.

In spite of the favorable outlook, risks to the growth projections are tilted to the downside, associated with the likelihood of renewed geopolitical tensions, especially the on-going Israel-Palestine conflict, which might lead to new supply chain disruptions and higher international prices for food and energy.

4.2 Decision of the Monetary Policy Committee (MPC)

The MPC noted that in spite of the recent ease in inflationary pressures, inflation remains high. While the Committee expects the downward trend to continue, it acknowledged the upside risks to the outlook, including an increase in volatility of commodity prices, especially energy and food prices, and high inflation expectations. Hence, the need for the BSL to continue with monetary policy firmly focused on taming inflation, without hindering productive investment and economic growth.

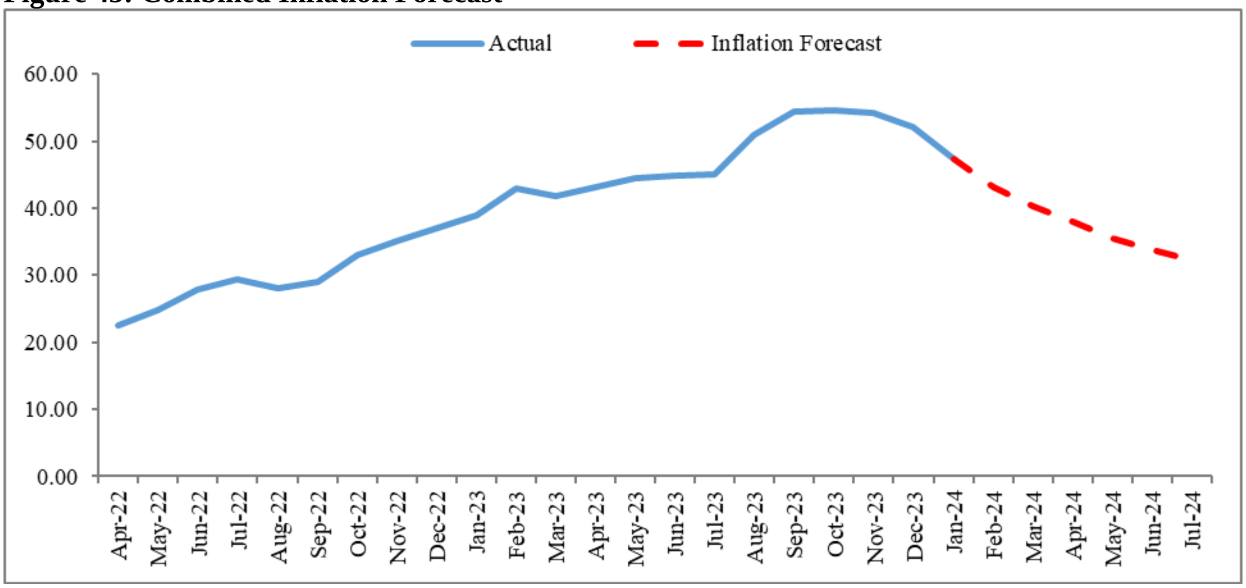
Consequently, based on its assessments of the risk to inflation, growth and financial system stability and the need to strike a balance between low inflation, strong growth and financial system stability, the MPC decided to increase the MPR by 1 percentage point to 23.25 percent. Accordingly, both the standing lending facility and the standing deposit facility rates were adjusted by the same margin to 26.25 percent and 16.75 percent respectively.

5. APPENDIX

Inflation Outlook

Inflation is projected to moderate in the near term. Combined forecast from a suite of forecasting models projects inflation to moderate to 32.3 percent by end July 2024. The Inflation forecast up to July 2024 is presented in the figure below.

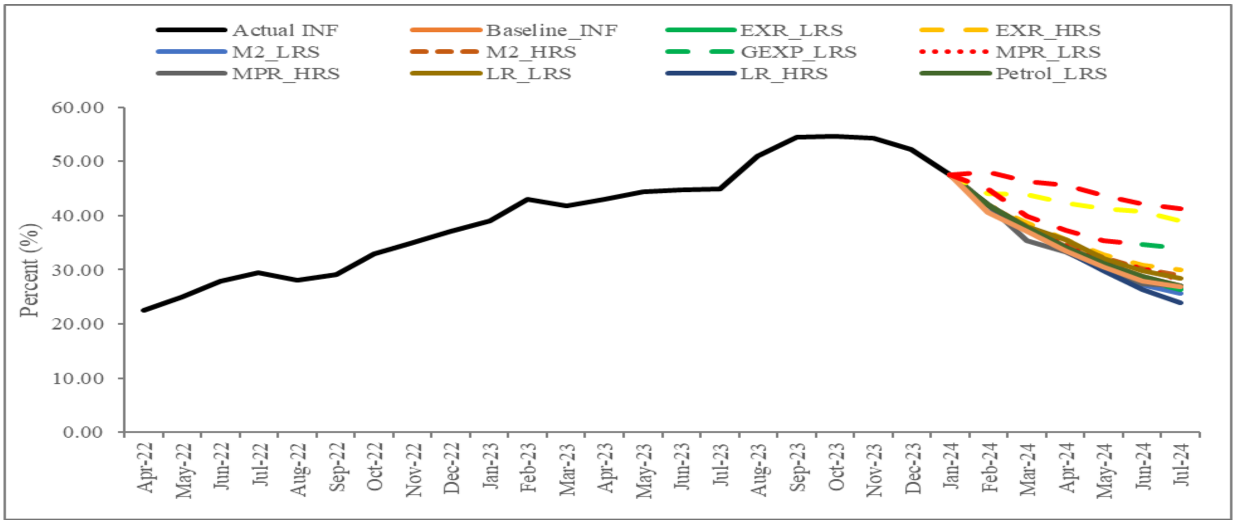
Figure 45: Combined Inflation Forecast



Source: BSL Staff calculations

Scenario analysis shows that additional increase in food and energy prices, in customs and excise taxes, depreciation of the exchange rate and monetary expansion would lead to higher inflation. On the other hand, a fall in food prices and reduction in money supply could slow down inflation.

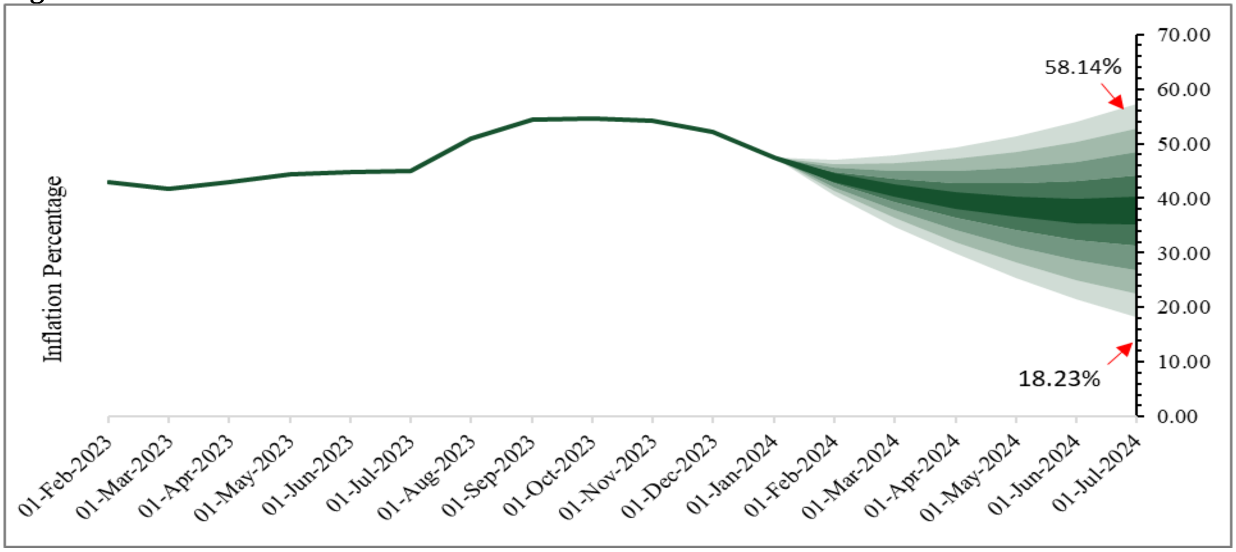
Figure 46: Combined Scenario Forecast



Source: BSL Staff calculations

The fan chart further indicates a 90 percent confidence interval that inflation will range between 58.1 percent and 18.2 percent within the forecast horizon.

Figure 47: Inflation Fan Chart



Source: BSL Staff calculations

Table 1: Summary of Global Growth Projections

	est	WEO October 2023 Projections		WEO January 2024 Projections		CHANGE IN Projections	
	2023	2024	2025	2024	2025	2024	2025
World Output	**3.1**	**2.9**	**3.2**	**3.1**	**3.2**	**0.2**	**0.0**
Advanced Economies	**1.6**	**1.4**	**1.8**	**1.5**	**1.8**	**0.1**	**0.0**
United States	2.5	1.5	1.8	2.1	1.7	0.6	-0.1
Euro Area	0.5	1.2	1.8	0.9	1.7	-0.3	-0.1
United Kingdom	0.5	0.6	2.0	0.6	1.6	0.0	-0.4
Japan	1.9	1.0	0.6	0.9	0.8	-0.1	0.2
Emerging Market and Developing Economies	**4.1**	**4.0**	**4.1**	**4.1**	**4.2**	**0.1**	**0.1**
Brazil	3.1	1.5	1.9	1.7	1.9	0.2	0.0
Russia	3.0	1.1	1.0	2.6	1.1	1.5	0.1
India	6.7	6.3	6.3	6.5	6.5	0.2	0.2
China	5.2	4.2	4.1	4.6	4.1	0.4	0.0
Sub-Saharan Africa	**3.3**	**4.0**	**4.1**	**3.8**	**4.1**	**-0.2**	**0.0**
Nigeria	2.8	3.1	3.1	3.0	3.1	-0.1	0.0
South Africa	0.6	1.8	1.6	1.0	1.3	-0.8	-0.3

Source*: IMF World Economic Outlook (WEO) October 2023 and January 2024 update.*

Table 2: Monetary Policy Stance of Selected Central Banks

Country	Recent Inflation (%)		Monetary Policy Rates (%)				
			Current		Previous		Change
WAMZ							
Sierra Leone	42.59	Feb.24	23.25	Mar.23	22.25	Dec.23	1.00
Nigeria	29.9	Jan.24	22.75	Feb.24	18.75	Jul.23	4.00
Ghana	23.5	Jan.24	29.00	Feb.24	29.00	Jan.24	0.00
Guinea	9.3	Dec.23	11.00	Jan.24	11.00	Dec.23	0.00
Liberia	10.4	Dec.23	20.00	Jan.24	20.00	Oct.23	0.00
The Gambia	16.15	Jan.24	17.00	Jan.24	17.00	Dec.23	0.00
Major Economies							
USA	3.4	Dec.24	5.50	Jan.24	5.50	Nov.23	0.00
China	(0.8)	Jan.24	3.45	Jan.24	3.45	Nov.24	0.00
Euro Area	2.8	Jan.24	4.50	Jan.24	4.50	Dec.23	0.00
UK	6.7	Sep.23	5.25	Jan.24	5.25	Dec.23	0.00

Source: Central Banks through Trading Economics

Table 3: Central Bank Survey

Millions of Leones	2023		Quarterly % Change		Yearly % Change	
	2023Q3	2023Q4	2023Q3	2023Q4	2022Q4	2023Q4
1. Net Foreign Assets	**(4,689.31)**	**(3,837.24)**	**55.42**	(18.17)	1,648.96	29.58
2. Net Domestic Assets	**11,928.40**	**12,550.90**	**15.22**	**5.22**	88.92	39.23
Government Borrowing (net)	9,937.48	9,896.82	**15.97**	**(0.41)**	62.76	37.97
o.w. Securities	4,190.85	5,324.74	**3.10**	**27.06**	232.97	44.04
Ways and Means	267.76	186.02	**10.48**	**(30.53)**	(39.86)	57.66
GoSL/IMF /WB Budget financing	4,874.75	4,224.70	**22.02**	**(13.34)**	4.91	19.65
3. Reserve money	**7,239.09**	**8,713.66**	(1.32)	**20.37**	31.53	43.95
o.w. Currency issued	6,002.65	7,148.62	(4.99)	**19.09**	31.07	42.51
Bank reserves	1,230.14	1,557.30	**21.66**	**26.59**	34.10	50.81

Source: Bank of Sierra Leone (BSL)

Table 4: Monetary Survey

Billions of Leones	2023		Quarterly % Change		Yearly % Change	
	2023Q3	2023Q4	2023Q3	2023Q4	2022Q4	2023Q4
Reserve money	**7,239.09**	**8,713.66**	**(1.32)**	**20.37**	**31.53**	**43.95**
Broad Money (M2)	**24,627.05**	**27,095.82**	**8.81**	**10.02**	**41.74**	**32.83**
Narrow money (M1)	**10,921.88**	**11,978.43**	**2.47**	**9.67**	**20.71**	**31.61**
Currency outside banks	5,321.61	6,178.16	**(6.43)**	**16.10**	**31.88**	**34.63**
Demand deposit	5,600.26	5,800.27	**12.65**	**3.57**	**11.15**	**28.54**
Quasi money	**13,705.17**	**15,117.39**	**14.45**	**10.30**	**64.89**	**33.82**
o.w. Foreign currency deposit	9,421.08	10,647.59	**19.48**	**13.02**	**104.94**	**40.27**
Time and saving deposit	4,277.79	4,462.05	**4.78**	**4.31**	**17.80**	**20.53**
Net Foreign Asset	**3,738.12**	**6,323.56**	**(16.54)**	**69.16**	**51.56**	**19.80**
BSL	(4689.31)	(3837.24)	**55.42**	**(18.17)**	**1648.96**	**29.58**
ODCs	8427.43	10160.80	**12.42**	**20.57**	**125.62**	**23.31**
Net Domestic Assets	**20,888.92**	**20,772.26**	**15.06**	**(0.56)**	**38.61**	**37.38**
Net Domestic Credit	**23,626.33**	**23,853.56**	**10.88**	**0.96**	**30.61**	**37.73**
Government (Net)	19,714.81	19,610.06	**12.55**	**(0.53)**	**34.27**	**40.60**
BSL	9937.48	9896.82	**15.97**	**(0.41)**	**62.76**	**37.97**
ODCs	9777.33	9713.24	**9.27**	**(0.66)**	**13.28**	**43.38**
Private Sector Credit	4116.71	4423.83	**5.80**	**7.46**	**11.93**	**25.00**
o.w ODC	4099.82	4404.75	**5.85**	**7.44**	**12.05**	**24.99**
Other Sectors (Net)*	(205.20)	(180.33)	**105.86**	**(12.12)**	**(42.14)**	**7.80**
Other Items (Net)	**-2,737.40**	**-3,081.29**	**(13.20)**	**12.56**	**(6.49)**	**40.10**
Money Multiplier	3.40	3.11				

Source: Bank of Sierra Leone (BSL)

Table 5: Combined Inflation Forecast

Months	Forecast
Feb-24	43.16
Mar-24	40.27
Apr-24	38
May-24	35.52
Jun-24	33.75
Jul-24	32.31

Source: BSL Staff projections

Table 6: Interest Rates

	2022	2023											
	Dec	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**
91-day T-bills	8.44	8.44	8.44	8.44	8.44	4.11	4.11	4.11	4.11	4.11	4.11	4.11	4.11
182-day T-bills	13.21	13.21	13.21	13.43	13.43	10.49	13.21	13.21	13.21	14.44	14.44	18.2	18.2
364-day T-bills	28.23	28.26	28.27	28.28	28.3	28.24	28.28	28.44	29.03	29.13	29.35	31.07	34.71
Interbank rate	18.9	19.47	19.82	20.26	20.8	20.89	20.99	21.31	21.80	21.89	22.87	22.86	24.75
SLF	21.25	21.25	21.25	21.25	21.8	21.75	21.75	22.25	22.25	22.25	24.25	24.25	25.25
SDF	12.25	12.25	12.25	12.25	12.8	12.75	12.75	12.75	12.75	12.75	14.75	14.75	15.75
MPR	18.25	18.25	18.25	18.25	18.8	18.75	18.75	19.25	19.25	19.25	21.25	21.25	22.25
Ave. Lending rate	20.095	20.14	20.14	20.18	20.4	20.445	20.32	20.45	20.45	20.45	20.45	20.45	20.19
Lending (Prime)	19.60 - 20.59	19.68 - 20.59	19.68 - 20.59	19.62 - 20.74	19.66 - 21.23	19.66 - 21.23	19.41 - 21.23	19.66 - 21.23	19.66 - 21.23	19.66 - 21.23	19.66 - 21.23	19.66 - 21.23	19.54-20.83
Savings deposits	2.17	2.17	2.17	2.17	2.2	2.17	2.23	2.23	2.23	2.23	2.23	2.23	2.34
Interest rate spread	17.97	17.97	18.01	18.28	18.3	18.09	18.09	18.22	18.22	18.22	18.22	18.22	17.84