

Speech by the Governor

Mr Momodu L Kargbo

Governor
Bank of Sierra Leone

at the

**Governor's Business
Lunch**

given at the

**Bank of Sierra Leone
Staff Recreational Complex
Kingtom, Freetown**

On

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His Excellency, The President,
Cabinet Ministers,
The Honourable Speaker and Members of
Parliament,
His Lordship, the Acting Chief Justice,
Your Worship, the Mayor of Freetown,
Chairman, Western Area, Rural District
Council,
Your Excellencies, Members of the
Diplomatic and Consular Corp,
Chief Executives of Commercial Banks
and Other Financial Institutions,
Representatives of the Private Sector,
Distinguish Ladies and Gentlemen.

Today we are fortunate to be able to gather here to mark the 51st anniversary of the Bank of Sierra Leone. This time last year, we could not celebrate the Bank's 50th anniversary, an important milestone in the history of the Bank, due to the Ebola outbreak. The Governor's annual dinner,

which usually provides opportunity to interact with stakeholders was not hosted.

Around this time last year, the country was reeling under the double blows of the EBOLA virus disease and the collapse of global prices of iron ore, which contributed to the closure of the two big iron ore mining companies and created uncertainty.

Today, Ebola is receding, the restrictions imposed to arrest the spread of the virus are gradually being eased and the air is filled with a ray of hope of a Post-Ebola Recovery. For us the monetary authority, this provides the opportunity to contribute to the normalization of our country and push the button of optimism to reinforce the resilience of Sierra Leoneans. I therefore encourage everyone to move on with renewed determination to chart a new path different from the past.

Mr. President Sir, Distinguished Guests, this business lunch provides a forum to engage with a cross-section of economic actors to set the stage for the themes, issues and actions for Post-Ebola planning and implementation; give some direction to the financial sector and galvanize all stakeholders into action in the post Ebola recovery. As we set about to kick-start the economy, which was moving at breakneck speed before the onset of the current crisis but has now slowed down, I wish to reassure you all that the Bank of Sierra Leone will work with commercial banks and other financial institutions to support and grow the economy.

A lot of issues and matters in the economic sphere give cause for concern. World commodity prices continue to be depressed. China is facing growth challenges and problems with their stock exchanges, potentially creating ripple effects around the world, especially the

developing countries that export to China. The current growth projection for Sierra Leone is somewhat pessimistic. I, however, would like to assure you all that from our assessment of the economy it is not all doom and gloom.

Mr. President Sir, Distinguished Guests, let me at this juncture provide you with highlights of macroeconomic developments since the outbreak of Ebola and the closure in the two mines. The economic shocks resulted in the erosion of business and investor confidence, reduced domestic revenue collection and increased Ebola related spending, placing considerable pressures on the budget. The suspension of mining activities had a domino effect on the services sector. As a result real GDP was 7 percent compared to a projected 11 percent. Inflation was moderate and remained in single digit during the year ending at 7.8 percent in December 2014, an improvement on the

8.2 percent for the same period in 2013. The Leone however, depreciated rapidly in 2014 by 12.0 percent compared to 0.5 percent in 2013, mainly due to the increased demand for foreign exchange required for the importation of medical equipment, fuel, and other essential supplies. There was also evidence of capital flight.

The financial sector was also affected. Banking hours were reduced and some banks closed operations in epicenters. Community Banks, Financial Services Associations (FSAs) and Microfinance Institutions (MFIs), which provide services in areas most affected, had to reduce operations or even close down. The evidence suggests that the effects of Ebola on the financial system were reduction in profitability of banks and other financial institutions, high default rate on loans and increase in Non-Performing Loans (NPLs).

Mr. President Sir, Distinguished Guests, against this backdrop, I now turn my attention to the **"Role of the Banking System in Post-Ebola Recovery and Beyond"**. The Bank of Sierra Leone has always supported growth and economic activities, by working with the Ministry of Finance and Economic Development to provide a stable macroeconomic environment. The Bank works tirelessly to deliver a safe and secure financial system for all. The Ebola outbreak of 2014 exposed the current system, bringing out weaknesses and vulnerabilities. These concerns provide opportunities for introspection, review and reforms, some of which I will elaborate on.

The Bank of Sierra Leone is under constant pressure to meet the growing foreign exchange needs of the country and the inactivity in the two major mining companies which had become major sources of foreign exchange for the

country, further exacerbated the problem. An important lesson to draw from this experience is the need to diversify the economy and create opportunities for other sources of earning foreign exchange. This issue of diversification is not only vital to increase foreign exchange flows but equally important in the broader scheme of development.

Linked to this matter of harnessing foreign exchange is the country's over dependence on import trade in finished consumer goods, which drains considerable amount of foreign exchange out of the country. This situation poses serious challenge for investment in the productive sectors, which provide avenues for employment generation and contribute to poverty reduction.

Mr. President Sir, Distinguished Guests, we are all too familiar with the present scenario; no venture capital, no angel

funds, a false start in the development of the stock exchange, the apparent unreliability of families and friends as source of raising funds for investment and the waning use of the "Osusus". Under such a scenario, the banking system will remain the focal point for meeting the credit needs of the private sector.

The investment needs in the Post-Ebola period are expected to increase significantly. The current high Non-Performing Loans (NPLs) which are intolerable, will create major difficulties if the causes of NPLs are not addressed. Among these are the lack of mutual trust and appreciation by the borrowers to present bankable proposals in order to obtain credit. It is incumbent that collective actions be taken to identify and resolve the bottlenecks in accessing finance particularly long-term finance in addition to strengthening the prudential guidelines in line with best practice.

Mr. President Sir, Distinguished Guests, permit me to throw the spotlight on the issue of Trust. Trust is fundamental to banking and financial operations. Many of the difficulties facing the financial sector are due to the erosion of trust between commercial banks and potential borrowers.

The high levels of Non-performing Loans and eventual default is a major challenge to the banks because they make these advances with customer deposits and in addition they have to make provisions for loans whose quality have deteriorated. Provisioning undermines their ability to make profit and this eventually threatens financial system stability and translates into high interest rates.

The common practice of borrowers securing a loan from a bank and not pay and then move on to another bank and

continue business as usual undermines financial stability. This practise is unacceptable and should be frowned upon by society.

On the basis of the above, the emerging inference suggests that, there may be culpability on the side of the banks and customers. Therefore, the need for trust is mutual and transcends all levels in the financial institutions and parties to banks' transactions. Regulations will be used to hold operational staff, management and boards of banks accountable for their actions.

A debt recovery bill is now being prepared and when enacted, could be used in combination with the bankruptcy law to make borrowers live up to their contractual obligations and spruce the country's banking habits. The underlying objective behind the intent to combine the use of the two laws is to eventually subject loan defaulters to judicial administration.

In this regard, the co-operation and collaboration of the Judiciary will be absolutely necessary.

The above points to the need for greater supervision of the operations of commercial banks by the Bank of Sierra Leone, the Boards of Directors and Shareholders of these banks to make them active partners that would play a positive role in the Post-Ebola Recovery Programme and beyond.

Mr. President Sir, Distinguished Guests, these commercial banks supported by the community banks and other financial institutions who are also involved in deposit taking and lending, are the foot soldiers and will be critical in the current mission. The primary function of these institutions is financial intermediation, which is the lifeblood of any economy, especially for production and growth.

The commercial banks and related institutions need to step-up their functions and activities to become viable contributors to the Post-Ebola Recovery Programme. For commercial banks to engage in effective intermediation they must be perceived by all parties as safe, sound, robust and reliable, especially depositors. This is both the responsibility of the central bank and the commercial banks themselves. The central bank provides the regulatory, legal framework, guidelines and other directives to ensure that commercial banks' operations are safe and sound and can meet the demands of their depositors and shareholders. Banks on the other hand are expected to set clear guidelines for assessing eligibility for loans and perform thorough due diligence to ensure recoverability.

This brings me to the case of two of the largest banks in the country which were ailing, putting to test the notion that banks

are safe and sound. In order to arrest the severe challenges facing these two banks, a resolution process spearheaded by the Ministry of Finance and Economic Development, National Commission for Privatization and the Bank of Sierra Leone is now in place charged with the responsibility of introducing safeguards to protect customers' deposits, instill confidence and to nurse the institutions back to normal operations. A key action under the resolution regime was the injection of capital into these banks. Ongoing work by the Resolution Regime is now focusing on identifying and resolving the underlying governance, management and institutional issues that gave rise to the challenges.

Early indication suggests that, the immediate threats to these banks may have been over. The accounts for 2014 for both banks were not qualified and one of them realized a small profit.

With all their problems, however, these banks have fundamental strengths such as a large and loyal customer base, deep reach and pricey real estate. These give them a very sturdy base. It is this strength that makes it imperative for these banks to be brought back to a healthy operational status to serve as a vehicle to channel resource in the Post-Ebola Recovery and beyond. Further, funding for SMEs is likely to be challenged until the issues of these two state owned banks are resolved.

Mr. President Sir, Distinguished Guests, liquidity in the banking system is very important for the effective functioning of the banking sector and to support economic activities. The commercial banks in general are already characterized by excess liquidity. A programme with the banks, which utilizes this excess liquidity to work for Post-Ebola Recovery and beyond is required. The excess liquidity

held in Government securities is not evenly distributed among the commercial banks. The interest rates on these instruments are considerably lower than lending rates but we observe that banks prefer to engage in "armchair banking" by investing in Government securities instead of intermediation for which they could make more profit. The banks on the other hand complain that there is a general lack of safe low risk projects to finance and that there is a high default rate among the potential borrowers, hence the decision to invest in risk free securities. However, as the central bank, the desire is to see liquidity evenly spread out across the banking system and some being utilised to support lending to the private sector.

Mr. President Sir, Distinguished Guests, financial inclusion, which for a long time has been under consideration, is now more relevant than ever. It is necessary to move to implement measures to make financial

services reach those that have been left out of the financial system - the so called unbankables. The Bank is currently considering various digital modes of financial inclusion to broaden outreach, especially in the rural areas. This will include mobile money transfer, use of internet banking, bank cards and other point of sale instruments. The proposed national switch is expected to be fully operational in a couple of years. This will provide a payment gateway that minimizes the need for cash transactions, replacing them with a more secure transaction platform by offering accessible and affordable electronic banking products. It will also expand services in general and specifically electronic payment products. Furthermore, it would eliminate long queues in banking halls; enable financial institutions to achieve economies of scale and bring about efficiency in financial service(s) delivery. With this system, customers will access funds from any

Automated Teller Machines (ATMs) or process transactions from any point of sale (POS) deployed at any shop, supermarket or fuel station or even their mobile phones. Digital banking therefore will increase the volume of loanable funds available in the banks for intermediation. Banks will become innovative and more aggressive in their customer drive by offering better services and incentives. The support of the Ministries of Energy and Power and Information and Communication will be required for 24 hours connectivity to ensure full customer utilization.

Mr. President Sir, Distinguished Guests, as part of the Post-Ebola Recovery response and to support the government's growth and employment objectives, the Bank of Sierra Leone will intensify the ongoing collaborative work with the Ministry of Trade and Industry, Ministry of Finance and Economic Development and the Office of the Chief of Staff to facilitate

and enhance growth, development and expansion of SMEs to undertake commercial activities focusing on production, processing and manufacturing. In that regard, work is underway to set up the relevant institution(s) such as an SME Agency to allow for funding, training technology acquisition etc. This will improve access to finance for SMEs to foster not only local production and trade but also job creation and exports.

Mr. President Sir, Distinguished Guests, complaints of high interest rates and the demands for collateral have been long outstanding issues. Current lending rates are considered too high and prohibitive for businesses to operate profitably and that the insistence on collateral to obtain loans hinders investment possibilities.

It must be reiterated that rates cannot be too low as banks have to cover their costs and not discourage intermediation.

However, to address this thorny issue of high lending rates, which is key if we are to increase access to finance and make it more affordable, the Bank of Sierra Leone has been engaging commercial banks in developing a base interest rate model as a guide to setting lending rates. The engagement is very far advanced and I am cautiously optimistic about the outcome.

On the issue of collateral, this is a necessary discomfort but an integral aspect of obtaining a loan from a bank. It facilitates the issuance of credit, provides assurance to the banks and make the borrower more committed to repay their loans. The enactment of the Borrowers and Lenders Act has expanded the range of assets that are acceptable to banks as collateral, including moveable properties.

A collateral registry is being set up at the Bank of Sierra Leone, and when operational will address the issue of a

single piece of collateral being used to guarantee multiple loans as the focus will be on the tradable value of the asset. Similarly, the credit reference bureau which was established a while ago will ensure that banks are informed of the credit history of potential borrowers to enable them to make better judgment relating to loan approvals.

Mr. President Sir, Distinguished Guests, the Apex Bank, Community Banks, Financial Services Associations (FSAs), Microfinance Institutions and Co-operative Societies also have a critical but unique role to play in providing finance to those outside the formal financial system mostly in the rural areas. These institutions by their nature have greater reach and traditionally lend to individuals and SMEs who may not meet the strict requirements for a commercial bank loan or may require smaller amounts of money to invest in their business activity. In

essence, these institutions should be supported to play a pivotal role in providing credit for small scale business entities, especially in rural communities or areas not covered by traditional commercial banks. These institutions would support inclusive and diversified growth which is needed for Post-Ebola recovery.

Mr. President Sir, Distinguished Guests, having said this, may I be the advocate for this very useful group of financial intermediaries, whose services could be relied upon to reach the small entrepreneur in the remote corners of the country to provide them with the necessary funds and technical support for growing their businesses. They must be partners in the Post-Ebola Recovery Programme and be provided with the necessary support to make them viable instruments.

We are happy that this lunch has brought together important stakeholders in the

financial sector. We have with us very senior government officials led by H.E. the President, representatives of financial institutions, private sector operators and, most important among us here today are the depositors and borrowers. As stakeholders we all play different roles in making the banking sector a vehicle for economic development.

As can be seen, the financial sector has a major role to play in the Post-Ebola Recovery period and beyond. It is incumbent on us to rise up to the occasion to take measures to make the necessary changes and introduce best practices to render the financial sector a capable partner in the economic development of the Country.

As a Central Bank, we will continue to work for a level playing field and set the stage by facilitating the enactment of the necessary laws and continually improve

the regulatory framework to ensure a viable, robust and development oriented financial sector. Above all, we remain committed to our traditional role of ensuring and maintaining monetary and financial stability.

Mr. President Sir, Distinguished Guests, I assure you all that, most of what you have heard here this early afternoon will not end here. Some are already in solid form by way of the continuing interaction between the Bank of Sierra Leone and the Banks through the Sierra Leone Association of Commercial Banks. It will be pursued with the Rural Finance Community Improvement Programme (RFCIP II) project funded by International Fund for Agricultural Development (IFAD), first by working to capacitate the APEX Bank and continually making representation to Government and Development Partners to not only provide capital for the existing Community Banks

and the Financial Services Association but working for their gradual and guided expansion. The interaction among the Ministry of Finance and Economic Development, the Ministry of Trade and Industry and the Office of the Chief of Staff around the development of SMEs in pursuit of the goal of diversification will be intensified.

In concluding can I draw from the buzz phrase at the launching of the Post-Ebola Recovery Programme and assure all that "It cannot be business as usual again in this Country" but more so in the financial sector.

Thank You.