Bank of Sierra Leone

MONETARY POLICY STATEMENT

At its 17th December 2020 meeting, the Monetary Policy Committee (MPC) of the Bank of Sierra Leone (BSL), under the Chairmanship of the Governor, Professor Kelfala M. Kallon, decided to reduce the Monetary Policy Rate (MPR) from 15.0 percent to 14.0 percent. The decision was informed by its assessment of developments in the domestic and international environment, and their potential implications for both macroeconomic and financial-system stability in Sierra Leone. The evidence that underpinned this decision are as follows:

I. INFLATION OUTLOOK

The MPC welcomed the deceleration in the inflation rate from 14.4 percent in June 2020 to 13.7 percent in September 2020, and further to 10.6 percent in November 2020. This was in part due to a sharp slowdown in food-price inflation following the BSL's support to the private sector for the importation of essential food items, the stability of the Leone in the foreign exchange market, and subdued domestic demand pressures.

Looking ahead, inflation is expected to continue trending downwards, with especially food-price inflation continuing to decline in the near term. This is due to the lag-effect of increased domestic food production during the harvest season on future food prices. Furthermore, the projected relative stability in the exchange rate and the moderation in world commodity prices (crude-oil prices especially) are expected to augment the favorable outlook for inflation in the coming months. Of course, whether this favorable inflationary outlook holds or not will depend on the magnitude of the supply-chain disruptions caused by the second wave of the COVID-19 Pandemic.

II. ECONOMIC GROWTH

A. Domestic Economic Growth

The domestic economy was projected to contract by 3.0 percent in 2020, reflecting the impact of the COVID-19 Pandemic, which continues to disrupt economic activity in key growth sectors of the economy. This notwithstanding, a modest recovery in the economic activity was observed in the Fourth Quarter of 2020, reflecting the lag-effects of the economic stimulus measures implemented by the BSL and the Government of Sierra Leone (GOSL) to mitigate the economic impact of the COVID-19 Pandemic. Furthermore, the likely resumption of iron-ore mining in the First Quarter of 2021, coupled with an improving global economic outlook, may strengthen domestic economic activity in the near term. Accordingly, domestic economic growth is expected to rebound to 2.7 percent in 2021.

B. **Global Economic Growth**

The October edition of the *World Economic Outlook* forecasts the global economy to contract by 4.4 percent in 2020, which is less severe than the 4.9 percent that was projected in the June 2020 edition. The revision was mainly due to a resumption in economic activities in May and June as most economies relaxed COVID-19-related restrictions, coupled with the ongoing monetary and fiscal stimulus measures implemented across the world.

In 2021, the global economy is expected to recover from the current global recession, and expectedly grow by 5.2 percent. However, whether the optimistic global and domestic economic outlooks that informed the MPC's decision materializes will depend, in part, on the longevity and severity of the current second wave of the COVID-19 Pandemic in the US and Europe.

III. THE EXTERNAL SECTOR

External sector performance improved during the Third Quarter of 2020, resulting in the narrowing of the trade deficit from US$272.0 million in the Second Quarter to US$206.9 million in the Third Quarter. This development resulted from the combined effects of an increase in export revenues and a decrease in import payments. Accordingly, the gross international reserves increased from US$681.5 million in the Second Quarter to US$738.1 million in the Third Quarter, which is sufficient to cover 5.8 months of imports.

The Leone-US dollar exchange rate remained relatively stable in the Third Quarter of 2020, partly due to the impact of the BSL's administrative measures to sanitize the foreign exchange market. Furthermore, the increase in inflows from development partners to support the fight against the COVID-19 Pandemic and the foreign exchange made available under the BSL's Special Credit Facility helped to keep the exchange rate relatively stable.

IV. FISCAL POLICY

Fiscal pressures eased during the Third Quarter of 2020, due to a significant inflow of foreign exchange resources from development partners as budget support to the Government—ostensibly to mitigate the impact of the COVID-19 crisis on the budget. Accordingly, the fiscal balance recorded a surplus of Le179.55 billion in the Third Quarter of 2020, which was much smaller than the Le530.35 billion in the Second Quarter. The MPC noted that the easing of the Inter-District Lockdown, the prospect of the resumption of iron-ore mining (which may help enhance domestic revenue mobilization), and an increase in expected donor support may collectively further ease fiscal pressures on the budget.

V. MONEY AND BANKING

In line with the increase in inflows from development partners, all of which were immediately monetized, monetary aggregates expanded during the Third Quarter of 2020. However, credit to the private sector remained constrained by the high bank lending rates and increased risk aversion by commercial banks in the face of uncertainty in the business environment due to the COVID-19 Pandemic. With the slowdown in COVID-19 infection rates and the gradual pick up in domestic economic activity, the MPC expects private sector credit to gradually recover in the near term, supported by the BSL's Special Credit Facility.

Money market liquidity has increased substantially as a result of increased inflows from development partners to support the government's programs to contain the economic fallout from the COVID-19 Pandemic and the payment of arrears of private-sector government debt.

A consequence of this development is that the interbank market rate declined to 12.1 percent in September 2020—from 17.7 percent in June 2020. A similar trend was observed in the Treasury Bill rates.

The MPC expects the current liquidity conditions in the banking system to enhance credit to the private sector to support the economic recovery process.

VI. FINANCIAL SYSTEM STABILITY

The MPC noted that the banking system continues to be resilient as evidenced by improvements in key financial soundness indicators and minimum systemic risks. However, the non-performing loans (NPL) ratio, though declining, remained above the prudential limit.

VII. CONCLUSION

Having considered the assessment of current economic conditions, the outlook for the economy in the near future (in particular, the expected favorable inflation outlook), and the need to continue to support economic recovery, the MPC agreed to cut the Monetary Policy Rate (MPR) by 100 basis points from 15.0 percent to 14.0 percent. This should serve as a signal to commercial banks to reduce their lending rates further in order to boost private-sector demand for credit. In addition, the Standing Lending Facility rate was adjusted downward from 19.0 percent to 17.0 percent and the Standing Deposit Facility rate from 10.0 percent to 8.0 percent. The Committee will continue to closely monitor price developments and stand prepared to take appropriate actions where necessary to maintain price and financial-system stability.

Furthermore, to mitigate the expected negative impact of the second wave of the COVID-19 Pandemic on the economy and simultaneously support the GOSL's medium-term food self-sufficiency program, the MPC agreed to propose to the Board of Directors of the BSL a low-interest 100 billion Leones Medium-term Lending Facility for financing the production, procurement, and distribution of agricultural implements and inputs. It is hoped that the long-term impact of this initiative on domestic food production will reduce the importation of rice, which will help to achieve the Bank's price and exchange-rate stability objectives.

Effective Monday, 28th December 2020, the following rates are published for the information of the public:

Monetary Policy Rate (MPR): 14.0 percent

Standing Deposit Facility Rate (SDFR): 8.0 percent

Standing Lending Facility Rate (SLFR): 17.0 percent

Professor Kelfala M. Kallon
Governor