# BANK OF SIERRA LEONE MONETARY POLICY FRAMEWORK

## 1. MONETARY POLICY OBJECTIVES

The primary objective of the Bank of Sierra Leone's (BSL) monetary policy is price stability. The BSL's mission therefore is to "formulate and implement monetary and supervisory policies to foster a sound economic and financial environment. Section 52(1) of the Bank of Sierra Leone Act 2019 stipulates that "in promoting price stability,the Bank shall pursue a monetary policy which serves the interest of Sierra Leone in accordance with the objective of the Bank". The BSL is accountable to parliament and the wider public. The legislation provides that monetary policy of Sierra Leone shall be formulated and implemented autonomously by the BSL.

## 2. THE MEDIUM-TERM INFLATION TARGET

Although Sierra Leone does not practice inflation targeting framework, yearly inflation targets are set under the IMF-ECF program. At operational level, there is a modeling team in the Research and Statistics Department of BSL supported by the Monetary Policy Department (MPD) that provides inflation forecast to guide the conduct of monetary policy in the near-to-medium-term. With technical support from the IMF, the modeling team at BSL has developed a suit of models for forecasting inflation. These models are based on key macroeconomic indicators which contain assumptions about future inflation. The inflation forecast complement the professional judgment of the MPC to assesses inflation outlook. In effect, the BSL uses forward looking approach to guide the conduct of monetary policy management.

## 3. THE MONETARY POLICY FRAMEWORK

The monetary policy framework of the BSL is primarily a monetary targeting framework, although the BSL operates a hybrid system. Under the hybrid system, the BSL combines traditional monetary targeting with a forward-looking monetary policy approach. The monetary targeting framework focuses on the growth rate of monetary aggregates – a measure of the quantum of money supply. The operational target is reserve money, while the intermediate target is broad money, and the ultimate target is inflation. The monetary targeting framework is based on the premise that in the long term, price growth is affected by price growth.

The forward-looking approach to monetary policy is implemented through an interest rate corridor system. In this corridor, there is lower band, which is the standing deposit facility – the overnight rate at which commercial banks with excess liquidity can deposit excess funds with the BSL, while the upper band, which is the standing lending facility – the overnight rate at which commercial banks can borrow from the BSL. The standing deposit and standing lending facilities can be symmetrical or asymmetrical to the MPR. The overall objective of the corridor system is to enhance liquidity management in the interbank market by steering interest rates in the wholesale market and thus the retail markets. In general, it is expected that monetary policy decisions would have an impact on the cost of credit, the amount of credit available and commercial banks decisions on credit allocation. Monetary policy typically reflects expectations about the outlook for inflation and economic activity and would therefore affect asset prices, exchange rates, consumption and investment, among other variables.

## 4. MONETARY POLICY COMMITTEE (MPC)

Section 14(2b) of the Bank of Sierra Leone Act 2019 prescribes that there shall be a Committee of the Bank to be known as the Monetary Policy Committee (MPC) which shall advise on any issue relating to the formulation of Monetary Policy and Monetary Policy Operations of the Bank. The membership of MPC consist of:

- The Governor
- Deputy Governor for Monetary Stability
- Deputy Governor for Financial Stability
- Four other experts with relevant professional experience in monetary policy and financial market operations. The four other experts are nominated by the Governor for a three-year term renewable once, subject to the approval of the Board of Directors of the BSL and should meet the eligibility criteria as set in Section 8 of the BSL Act 2019.

The Governor of the BSL is the Chairman of the MPC and the meetings are held quarterly. In the absence of the Governor, the Acting Governor of the BSL serves as the Chair of the MPC meetings. Four members including the Chairman of the MPC constitute the meeting quorum. Decision-making takes place by vote, with the Chairman having a deciding vote in case of a tie.

## 5. MONETARY POLICY COMMUNICATION

The MPC ensures that the BSL's monetary policy, operations, and outcomes are communicated in line with the IMF's Central Bank Transparency Code (2020). In that regard, several initiatives have been undertaken to improve the communication of monetary policy stance to the public. At the conclusion of every MPC meeting, a Monetary Policy Statement containing the decision on the Monetary policy Rate and its underpinning considerations is published on the Bank’s website, in the electronic and print media and the printouts sent to key stakeholders. The MPC decision is also presented to commercial banks in the Bankers' Association meeting with the Bank. Going forward, a press conference will be held by the Governor of the BSL to explain the reasons for the MPC's decisions. It is expected that this press conference will be broadcasted live on national television.

## 6. MONETARY POLICY IMPLEMENTATION

Monetary policy is implemented by the Open Market Operations Committee which is responsible for the implementation of monetary policy. The Committee is chaired by the Director of the Financial Markets Department and include other key departments (Research and Statistics department, Monetary Policy Department, Banking and Payments System Department and Financial Markets Department).

## 7. MONETARY POLICY INSTRUMENTS

The instruments of monetary policy are Open Market Operations (OMOs), Reserve Requirement, Foreign Exchange Intervention and Moral Suasion.

**7.1 Open Market Operations**. This involves the purchases and sales of Government Treasury securities in the secondary market. The operations take the following forms:

### 7.1.1 Repurchase Agreement (Repo)

Repo is a contractual agreement where the BSL sells eligible securities, such as the Sierra Leone Government securities to banks and Discount Houses and at the same time, commits to repurchase the same securities on a specified date at a specified price which reflects the repo rate. Repo is used to temporarily absorb liquidity from the banking system, for a fixed period of time agreed between counterparties. Ownership title to the securities during the repo period transfers to the provider of resources (funds).

On the other hand, the Reverse repo, is a contractual agreement where the Bank buys eligible securities from banks and discount houses and commits to resell the same securities on a specified date at a specified price. The Bank uses reverse repo transactions to inject liquidity into the banking institutions.

### 7.1.2 Outright Sale/Purchase of Government Securities

The BSL may perform an outright sale or purchase of Government securities address liquidity challenges in the banking system.

An outright transaction implies a full transfer of ownership from the seller to the buyer with no reverse transaction, and as such, the operations have a permanent effect on money market liquidity. The operational features of outright transactions could be summarized as follows:

- They can take the form of liquidity-injection where there is a structural deficiency (outright purchase) or liquidity- absorption where there is a structural excess liquidity (outright sale) operation.
- Their frequency is not predetermined but depends on the need.
- Their execution is conducted through an auction/tender system.

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### 7.1.3 Standing Facilities

In the event of residual surpluses or shortages, the Bank makes available the overnight standing facility, at the instance of the commercial banks. Request for access to the standing facilities must be made to the BSL by the interbank institutions before 4:30 p.m. Interbank institutions would access this facility when there are unforeseen factors that result in surpluses or shortages relative to their minimum reserve or settlement requirement, late in the day and cannot be covered via the normal money market transactions. The interest paid on overnight deposits is the floor rate (x basis points below the MPR) while interest charged on overnight lending is the ceiling rate (x basis points above the MPR). In a liquidity shortage scenario, all lending operations are conducted in the form of a repo. Eligible securities for these transactions are the Government and/or Central Bank securities.

### 7.1.4 BSL Intra-Day Liquidity Facility (ILF)

The Bank also provides liquidity via the Intra-Day Liquidity Facility window during the day at the instance of commercial banks at zero cost to ensure smooth operations of the RTGS system. Commercial banks accessing this window should ensure their accounts are adequately funded to reverse the transaction by close of the working day. ILF is automatically converted into an overnight credit at the Standing Facility Rate and against eligible securities, if the counterparty fails to settle on the same day.

Commercial banks should submit their Intra-Day Facility request through the CSD System from start of business day, but not later than 15.30hr.

### 7.2 Foreign Currency (FX) Transactions

The Bank may conduct foreign currency wholesale auction to smoothen volatility in exchange rate as well as absorbing or injecting liquidity. With wholesale FX transactions, the Bank may either purchase or sell foreign currency in the interbank market.

### 7.3 Statutory Reserve Requirement (SRR)

The Statutory Reserve Requirement (SRR) is an instrument used to limit monetary expansion as well as manage liquidity. Banking institutions are required by law to maintain a minimum balance equivalent to 12 percent of their local currency deposit liabilities at the BSL and this is averaged over a maintenance period of 28 days..

## 8. DAILY OPERATIONS

The Bank's daily monetary operations are conducted between **8:00am to 4:30pm**, executed via various combinations of monetary instruments. See attached **Appendix 3**.

Liquidity position in the banking system is established daily through liquidity forecasting to inform/guide the conduct of monetary operations. The forecast is based on analysis of various factors, including the maturity of previous securities issued by the Government, repo transactions, changes in currency in circulation and large payments in and out of Government Treasury accounts. Both the overnight deposit and lending facilities are made available to the interbank institutions in the evening to manage any surplus or deficit of liquidity in the system for the day. All approved interbank institutions are able to participate directly in Open Market Operations (OMOs) conducted by the Bank including Standing Facilities.

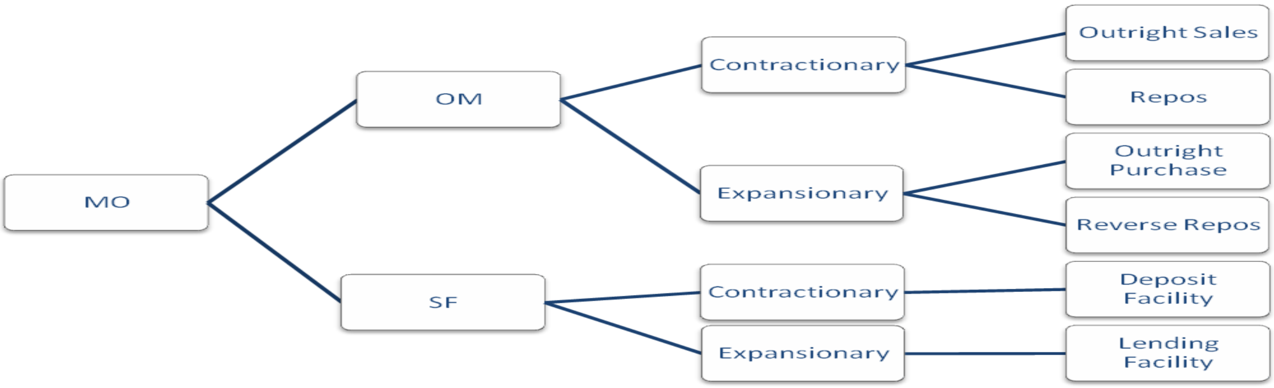
## 9. OTHER COMPLEMENTARY MONETARY POLICY TOOLS

Going forward, BSL will consider adopting other complementary instruments such as, BSL securities for liquidity management and macroprudential tools to enhance the conduct of monetary policy management.

## 10. RISK MANAGEMENT

When the Bank lends in its operations, it does so against collateral of sufficient quality and quantity to protect itself from counterparty credit risk. All interbank institutions are holders of eligible securities that are used as collateral in the money market. All collaterals have a "haircut" applied. This is a discount to the value of assets to protect the Bank against loss should a counterparty fail to repay. Currently, a haircut of 10% is applied on all eligible securities. As the market evolves, the Bank will continue to review the breadth of collateral eligible for use in its facilities.

**Appendix 1:  Layout of Monetary Operations of Bank of Sierra Leone**




**Where:-**

**MO - Monetary Operations**

**OM - Open Market**

**SF - Standing Facilities**

**Appendix 2: Description of Standing Facilities**

| **Description** | **Deposit Facility** | **Lending Facility** |
|---|---|---|
| Liquidity Impact | Tighten liquidity | Expand liquidity |
| Frequency of Transactions | Daily/Regular | Daily/Regular |
| Tenor | Overnight | Overnight |
| Minimum Bid Amount | Le1,000,000 | Le1,000,000 |
| Multiples of Bid Amount | Le5.0mn | Le5.0mn |
| Settlement | DVP | DVP |
| Bidders | Commercial banks | Commercial banks |

## Appendix 3: Framework of Daily Monetary Operations