Bank of Sierra Leone

MONETARY POLICY STATEMENT – 5TH APRIL 2022

The Monetary Policy Committee (MPC) of the Bank of Sierra Leone (BSL) met on 30th March 2022 under the Chairmanship of the Governor, Professor Kelfala M. Kallon. After a thoughtful assessment of recent global and domestic macroeconomic developments and their implications for price and financial stability in Sierra Leone, it decided to raise the Monetary Policy Rate (MPR) by 75 basis points to 15.0 percent. Below are the evidence that informed the Committee's decision:

Inflation

Based on the rebased Consumer Price Index (CPI) produced by Statistics Sierra Leone, headline inflation increased from 11.63 percent in 2021Q3 to 17.94 percent in 2021Q4. Thereafter, it moderated to 16.65 percent in January 2022. However, it picked up in February 2022 to 17.59 percent. Global commodity-price inflation (especially fuel and food), high freight charges, the overall global negative supply shock created by the Russian-Ukranian crisis, and the uncertainties surrounding the COVID-19 pandemic suggest that inflationary pressures are expected to persist in the near period. The resultant increase in domestic fuel pump prices, which is bound to raise production costs economywide, may most likely impose adverse consequences for domestic prices. In short, inflationary pressures are likely to persist in the near term.

Domestic Economic Growth

Domestic economic activity picked up in 2021, but at a slower pace than previously expected. Real gross domestic product (RGDP) growth in 2021, which was estimated at 3.2 percent, was downgraded to 2.9 percent. This subdued economic performance was also reflected in the BSL's high frequency indicator of economic activity—the Composite Index of Economic Activity (CIEA), which shows that the economy contracted by 2.73 percent in 2021Q4.

RGDP growth is expected to be stronger (at 5.0 percent) in 2022, supported by an expected increase in activities in the agriculture, manufacturing, services and mining sectors. However, the Russia-Ukrainian crisis and the ensuing sanctions regime that Western Powers have imposed on Russia, have heightened global economic uncertainty, which could significantly weigh on global economic recovery and commodity markets. This may have an adverse impact on economic growth, especially for small open economies like Sierra Leone. In short, actual RGDP growth during 2022 may, more likely than not, fall below its forecasted value of 5.0 percent.

Global Economic Growth

Based on the January 2022 edition of the IMF's *World Economic Outlook (WEO)*, Global growth is expected to moderate from 5.9 percent in 2021 to 4.4 percent in 2022. This prediction is largely based on reduced growth forecasts for the two largest economies—the USA and China. Because China is an increasingly important trading partner of Sierra Leone, the downward revision in its growth rate will most obviously adversely impact the Sierra Leone economy.

Accordingly, risks to global growth in 2022 are tilted to the downside, as the Russian-Ukrainian Crisis and its ensuing sanctions have heightened global economic uncertainty. Coupled with the COVID-19-induced negative supply shock to the global supply chain, these shocks are expected to lower RGDP growth to 3.8 percent in 2023. Nevertheless, this is an increase of 0.2 percent when compared with the previous forecast in the October 2021 edition of the *WEO*.

External Sector

External sector performance was mixed in 2021Q4**.** The trade deficit widened from US$ 146.65 million in 2021Q3 to US$245.66 million in 2021Q4. This is due to the combined effects of increased imports and decreased exports.

The stock of gross foreign exchange reserves of the Bank of Sierra Leone (excluding swaps) decreased from US$932.90 million in 2021Q3 to US$931.76 million in 2021Q4. This was singularly due to a revaluation loss of US$4.24 million outweighing the net inflows of US$3.10 million. Despite the decrease, the stock of reserves was enough to cover about 5.4 months of imports of goods and services.

Resultantly, the Leone continued to depreciate against major international currencies in 2021Q4, due to reduced supply of foreign exchange in the face of increased demand. This pressure is likely to increase during the Ramadan period, which is characterized by increased import demand for food and other essential commodities. Additionally, as worldwide COVID-19 travel restrictions are eased, the demand for foreign exchange for international travel is likely to increase, thereby putting greater pressure on the Leone's international exchange value.

The MPC noted the reduced supply of foreign exchange from exports, foreign direct investments and other sources of inflows in the face of increased demand for the importation of essential goods especially fuel and food. In particular, given the high unfulfilled demand for foreign exchange for the importation of key commodities (most prominently, fuel and food), the Committee is of the view that the demand pressures will lead to a significant depreciation of the Leone in the near future. Given the high pass-through effects of exchange rate depreciation on domestic prices, this will lead to higher prices, which will potentially negatively impact living standards of especially the poor. To mitigate against this, the MPC recommends that the Board of Directors creates two Special Facilities for food items (rice, flour and sugar) and fuel, respectively, that would provide foreign exchange for the importation of these items.

The MPC also noted that the current wave of exchange rate depreciation is not unique to Sierra Leone. The weekly exchange rate analysis by the BSL for the West African Monetary Zone (WAMZ) countries (The Gambia, Ghana, Liberia, Nigeria, and Sierra Leone) shows that exchange rate depreciation in Sierra Leone is similar to what is currently obtaining in most member states in the WAMZ. The MPC is of the view that the current wave of exchange rate depreciation in the Zone will continue until the issues of rising global commodity prices, global supply chain disruptions, high freight charges and the COVID-19 pandemic are addressed at the global level.

Fiscal Policy

Fiscal operations improved in 2021Q4, as the fiscal balance improved from a deficit of Le1.06 trillion in 2021Q3 to a surplus of Le439.55 billion in 2021Q4. This reflected an improvement in government revenue mobilization and a contraction in government expenditure. The primary balance also narrowed from a deficit of Le535.30 billion in 2021Q3 to a deficit of Le321.67 billion in 2021Q4.

Despite this improvement, the MPC noted that total revenue and grants was lower than its target for 2021Q4. Given the expenditure requirement to support Government's economic recovery program, the MPC is of the view that further fiscal consolidation efforts are needed. This plus the expected donor inflows and the SDR allocation that the BSL will make available to Government may help to improve the fiscal outlook in 2022.

Money and Banking

Growth in monetary aggregates expanded in 2021Q4, reflecting in part the inflows from the IMF and other development partners. Similarly, growth in private sector credit expanded from 3.51 percent in 2021Q3 to 8.27 percent in 2021Q4. Despite this improvement, the MPC is of the view that the prevailing high bank lending rate remains a challenge for private sector investment and growth. However, it is expected that the Upgraded Collateral Registry could help to enhance credit to the private sector.

In the money market, the yields on Government securities continued to rise in 2021Q4, led by the 364-day T-bills. Also, the interbank rate continued to trend upwards in the review period, but remained within the Policy corridor.

Financial System Stability

The banking sector remains relatively stable as most of the key financial soundness indicators (FSI) remained above their minimum thresholds. However, the MPC noted that the Non-Performing Loans ratio (NPL) increased from 14.60 percent in 2021Q3 to 15.23 percent in 2021Q4, which may be partly due to the adverse impact of the economic downturn on the ability of borrowers to service their debt obligations. Relative to the regulatory limit of 10 percent, this high NPL ratio poses challenges for financial intermediation.

Conclusion

Inflationary pressures remain high, and it is expected to remain on its elevated path until its externally-induced causal factors (such as, rising global commodity prices, higher freight charges, disruption in global supply, uncertainty surrounding COVID-19 pandemic and the Russian-Ukrainian Crisis) are controlled. The above notwithstanding, the MPC views the current inflationary trend as a cause for concern. Consequently, mindful of the BSL's responsibility for safeguarding price and financial-system stability, while supporting economic growth, the MPC decided to raise the Monetary Policy Rate (MPR) by 75 basis points to 15.0 percent and adjust the Standing Lending Facility Rate and the Standing Deposit Facility rate upward by the same margin. Hence, effective 5th April 2022, the following rates are published for the information of the public:

Monetary Policy Rate is 15.0 percent
Standing Lending Facility Rate is 18.0 percent
Standing Deposit Facility Rate is 9.0 percent

Finally, in order to cushion the impact of the expected inflation on the living standards of the poor, as well as avoid shortages of key essential commodities in the economy, the MPC also recommends the creation of a Special Facility for Food (SFF) and a Fuel Reserve Facility (FRF) to provide foreign exchange resources, through the commercial banks, for the importation of rice, flour, sugar, and fuel.

The MPC will continue to monitor developments in the global and domestic macroeconomic and financial environment and stands ready to take appropriate actions should they adversely impact price and financial-system stability.

Professor Kelfala M Kallon
Governor