Bank of Sierra Leone

MONETARY POLICY STATEMENT

The Monetary Policy Committee (MPC) of the Bank of Sierra Leone (BSL) met on 24th and 25th June 2021 under the Chairmanship of the Governor, Professor Kelfala M. Kallon. After assessing developments in the domestic and international environments, the MPC decided to keep the Monetary Policy Rate (MPR) at 14.0 percent. The justifications for that decision are provided in the rest of this statement.

Inflation

Based on its assessment of relevant data, the MPC concluded that inflation is expected to be subdued in the near future, in spite of month-to-month gyrations. The Committee specifically noted that annual headline inflation moderated to a single digit in March 2021—to 8.95 percent from 10.45 percent in December 2021, the lowest in six years. However, inflation picked up marginally in the first two months of the second quarter, increasing to 9.60 percent in April 2021 and further to 9.80 percent in May 2021. The recent modest increase in inflation was largely driven by an increase in food prices, which pushed up the food inflation from 15.64 percent in April 2021 to 17.56 percent in May 2021. In contrast, non-food inflation moderated to 3.57 percent in May 2021 from 4.67 percent in April 2021. Though inflation increased in the early months of the second quarter, the MPC noted that it is still below the end-year target.

In the near term, the risks to the inflation outlook are tilted to the upside, driven largely by seasonal domestic food supply shocks as we enter the rainy season, the pass-through of higher global commodity prices to domestic prices, and the reemergence of uncertainty in the economy in the face of the new strains of COVID-19. However, the MPC is of the view these pressures should moderate over the near to medium-term, as policy support to the agriculture sector begins to take hold.

Domestic Economic Growth

The domestic economy continues to demonstrate signs of recovery, with real GDP growth projected to rebound to 3.2 percent in 2021 from a contraction of 2.2 percent in 2020. The expected improvement in the growth outlook is supported by expected recovery in the critical growth sectors (mainly agriculture, mining and services), coupled with higher public investment in infrastructure. In addition, recovery in global demand could support growth prospects in Sierra Leone through its impact on the demand for exports for primary commodities and increased inward flows of foreign direct investment (FDI). The MPC's optimism for economic recovery is further substantiated by the BSL's Composite Index of Economic Activity (CIEA) which shows that economic activity remains positive in the first quarter of 2021, though lower when compared to what obtained in the fourth quarter of 2020.

Moreover, the effective roll-out of the COVID-19 vaccines globally, and in Sierra Leone in particular, coupled with the supportive fiscal and monetary policy measures put in place, and the expected improvement in the global economic outlook could help to enhance business and consumer confidence, and thus stimulate economic activities. Whether these predictions materialize will expectedly depend on the severity of Third Wave of the COVID-19 Pandemic on both the domestic and global economies.

Global Economic Growth

The April 2021 edition of the *IMF World Economic Outlook* projects global growth to rebound strongly to 6.0 percent in 2021, compared with the contraction of 3.3 percent in 2020. However, it is expected to moderate to 4.4 percent in 2022. The optimistic growth projection in 2021 is mainly based on the gradual easing of restrictive measures, owing to an anticipated widespread vaccination against COVID-19, coupled with strong policy support by developed economies.

The MPC assessed that the recovery is expected to be uneven and likely to differ across countries, with the fortunes of each country depending on the extent of economic damage done by the Third Wave of COVID-19, the effectiveness of its policy response, and the severity of the health shocks. The downside risks to the growth outlook dominate, as for instance, the implementation of stiffer restrictive measures and their disruptive impact on economic activity may sap consumer and business confidence, thereby causing lower productivity to reemerge.

External Sector

External sector performance was mixed in the first quarter of 2021. Trade deficit widened to US$ 367.47million in 2021Q1 from US$203.08 million in 2020Q4, reflecting higher rate of growth of imports relative to exports. Although trade deficit widened, the MPC noted that Sierra Leone's external vulnerability remains moderate, partly due to the increase in its gross external reserves.

The exchange rate of the Leone in terms of the US dollar remains relatively stable, albeit with a marginal depreciation in the review period. The relative stability in the exchange rate is, in part, due to increased inflows from exports, remittances and FDI and a COVID-19-induced reduction in foreign travel. The BSL's Special Credit Facility, which provided foreign currency for the importation of essential commodities, also anchored expectations in the foreign exchange market. Above everything else, exchange rate movements are, by and large, determined by the differential between domestic and foreign inflation rates. As such, the downwardly trending domestic inflation rate played a major role in the observed relative stability of the Leone against foreign currencies.

Fiscal Policy

Fiscal pressures intensified during the first quarter of 2021, arising mainly from the juxtaposition of increased government expenditures with reduced government revenues. On the one hand, expenditures increased significantly to finance COVID-19 containment measures and other programmes that were implemented to support economic recovery and also provide support for the economically vulnerable members of society. On the other hand, the COVID-19-induced downward pressure on economic activity reduced government revenue. Consequently, both the budget deficit and the primary balance deteriorated during the review period.

The MPC expects fiscal pressures to continue in the coming quarters, given the resurgence of COVID-19 pandemic infections in recent months. However, increased efforts to mobilize external support, the expected disbursement under the IMF supported Extended Credit Facility, coupled with the enhanced domestic revenue mobilization drive in the remaining quarters of the year could help to moderate those fiscal pressures.

Money and Banking

Consistent with the fiscal stimulus and complementary monetary policy measures to mitigate the impact of the COVID-19 pandemic, monetary aggregates expanded in 2021Q1. The MPC welcomed the improvement in private sector credit, which expanded by 8.97 percent in 2021Q1, relative to 0.21 percent growth in 2020Q4. It also expects the improvement in private sector credit to continue, supported in part by the roll-out of the BSL's Agricultural Credit Facility.

Liquidity in the money market showed signs of tightness in 2021Q1, as reflected in the upward trends in the interbank market rate and treasury bill rates. The MPC expects that the disbursement of the funds under the IMF's Extend Credit Facility and other expected donor inflows could moderate government exposures in the money market in the near-term.

Financial System Stability

The MPC found financial sector performance during the period under review to have been generally satisfactory. The sector remains stable, resilient, adequately capitalized and profitable, with satisfactory level of liquidity. The Committee is however mindful of the fact that the quality of assets of commercial banks deteriorated during the period in question, with the non-performing loans increasing to 14.10 percent in 2021Q1 from 12.70 percent in 2020Q4.

The financial sector is expected to remain safe, sound, and operating in compliance with existing BSL policies and prudential and regulatory measures. Additionally, the BSL continues to monitor the quality of banks' assets with a view of reducing non-performing loans to the desired level of 10 percent.

Conclusion

Given that inflation is forecast to be around the end-year target and the economy is on a recovery path, coupled with the elevated uncertainty around the reemergence of the new strains of the COVID-19 virus, the MPC resolved that a cautious monetary policy stance is warranted at the moment to boost the momentum of the economic recovery and private sector credit growth. Consequently, the MPC unanimously decided to keep the Monetary Policy Rate, the Standing Lending Facility Rate, and the Standing Deposit Facility Rate unchanged.

The MPC will continue to assess the global and domestic economic developments and their implications on the overall inflation outlook and would respond appropriately should any development create inflationary expectations.

Hence, effective Monday 28th June 2021, the following rates are published for the information of the public:

Monetary Policy Rate (MPC): 14.0 percent

Standing Deposit Facility Rate (SDFR): 8.0 percent

Standing Lending Facility Rate (SLFR): 17.0 percent

Professor Kelfala M. Kallon
Governor