MINUTES OF THE MONETARY POLICY COMMITTEE MEETING

May 4 – 5, 2006

The twelfth meeting of the Monetary Policy Committee of the Central Bank of The Gambia was held in the Conference Room of the Bank on May 4, 2006.

Present:

Famara L. Jatta	-	Governor, (Chairman)
Momodou B. Saho	-	General Manager, Member
Basiru Njai	-	Director, ERD, Member
Ousman Sowe	-	Director, FSD, Member
Amadou Colley	-	Deputy Director, BSD, Member
Mod Secka	-	Deputy Permanent Secretary, DOSFEA Member
Buah Saidy	-	Deputy Director, ERD (Secretary)

In Attendance Were:

Oumie Samba-Savage	-	Director, FISD
H M V Carr	-	Director, AH
Omar Jatta	-	Deputy Director, FD
Essa Drammeh	-	Deputy Director, FSD
Haddy Joof	-	Deputy Director, AH
Ousainou Corr	-	Deputy Director, FISD
Pa Alieu Sillah	-	Commissioner of Insurance
Fatou Deen-Touray	-	Deputy Director, MFD
EAC Ndong	-	Principal Officer, FD
Paul Mendy	-	Principal Bank Examiner, FSD
Abdoulie Jallow	-	Principal Bank Examiner, FSD
Bakary Kolley	-	Senior Economist, ERD

Ismaila Jarju	-	Senior Economist, ERD
Bakary Jammeh	-	Senior Econometrician, ERD
Maimuna John-Sowe	-	Senior Economist, ERD
Karamo Jawara	-	Senior Banking Officer, BSD
Anita Riley	-	Senior Banking Officer, BSD
Halima Singhateh	-	Bank Examiner, FSD
Bernard Mendy	-	Bank Examiner, FSD
Momodou Lamin Jarjue	-	Banking Officer, BSD
Buba Touray	-	Statistician, ERD
Sait Mboob	-	Economist, ERD
Nyakassi Sanyang	-	Statistician, ERD
Sheriff Touray	-	Economist, ERD

Before turning to its immediate policy decision and against the background of output and inflation projections, the Committee discussed balance of payments developments, fiscal, money market, monetary, banking sector and international developments.

(1.0) Developments in the International Economy

Despite high and volatile oil prices, natural disasters, tightening in financial market conditions, and rising global imbalances, global activity remain strong. The global economy is forecast to grow by 4.9 percent, up from 4.3 percent earlier projected underpinned by stronger output growth in China, Russia, India and other emerging market economies.

In the United States, GDP growth is expected to moderate to 3.4 percent in 2006, still the highest among G-7 countries. Although the US economy experienced a surprisingly weak fourth quarter growth in 2005, data indicates a strong start in 2006. However, an abrupt slowdown in the housing market poses significant risk to the outlook.

Despite a slowdown in Q4, 2005, economic activity in the Euro zone picked up in the Q1, 2006. The Euro zone's manufacturing purchasing managers' index rose to 56.1 in March 2006 from 54.5 in February 2006, the highest reading since September 2000 reflecting in the main strong manufacturing output in Germany. With consumption remaining weak, the zone is vulnerable to domestic shocks.

China's economy grew at an annual rate of 10.0 percent in the Q1, 2006 on the back of accelerating exports and resurgent bank lending. Overall, GDP is expected to slow modestly to 9.5 percent in 2006, from 9.9 percent in 2005. China's external position continued to strengthen, and foreign exchange reserves increased by over $200 billion to almost US$800.0 billion in 2005. The fear is that given ample liquidity in the banking system, the economy may overheat unless monetary conditions are tightened.

In Japan, the economy continues to grow strongly causing inflation, land prices, and bank lending to rise. The improving labour market boosted consumption growth. The challenge facing Japan is how to normalize monetary and fiscal policies without halting the ongoing recovery.

Growth in the UK slowed to 1.8 percent in 2005, driven by a slowdown in consumption which, in turn, reflected the cooling of the housing market, earlier monetary policy tightening, and higher energy prices, business investment and export growth have remained steady.

Although output is expected to grow by 2.5 percent in 2006, the UK's purchasing managers' manufacturing index fell in March 2006, its lowest reading since August 2005. This reinforced expectations that UK rates will remain on hold for the time being.

The economic outlook in Sub-Saharan Africa (SSA) remains positive, with growth of 5.8 percent projected in 2006, the highest in over thirty years. The robust outlook is underpinned by high commodity prices, improved macroeconomic policies, and structural reforms in many African countries.

Financial conditions continue to be tightened. The US Federal Reserve raised the policy rate for the fifteenth time in a row by 0.25 percent to 4.75 percent in March 2006 and signalled that further increases might be needed to stem rising inflationary pressures.

In the UK, the Bank of England's Monetary Policy Committee kept interest rates on hold at 4.5 percent for the eighth month in a row. With inflation close to target and economic growth forecast to pick up, expectations are that rates will remain unchanged for the rest of 2006.

In April 2006, the People's Bank of China raised interest rates for the first time in 18 months in an attempt to slow rapid credit and investment growth. The benchmark one-year lending rate was raised, albeit slightly from 5.58 percent to 5.85 percent while the benchmark deposit rate was unchanged at 2.25 percent.

According to the IMF, prices of energy and non-oil commodities increased by over 29.0 percent in 2005. Energy prices rose by 39.0 percent reflecting marked increase in oil and natural gas prices. Prices of non-fuel commodities rose by 10.0 percent, reaching record highs in nominal terms. Robust economic growth and limited supply responses were mainly responsible for the acceleration in prices.

The Committee observed that the US, China and India remain the engines of global growth, while Japan has re-emerged from persistent deflationary pressures. It is encouraging that economic growth in the Euro area appears to be gaining traction, but the Committee warned that the zone may be vulnerable to external shocks because of global imbalances and the rising Euro.

The Committee welcomed the continued robust economic output in SSA, but noted that it is still not strong enough to meaningfully impact poverty. Besides, growth has been uneven and punctuated by recurring food insecurity and humanitarian crisis in some countries.

The Committee questioned the rationale by the Chinese authorities to target two policy rates. But the point was made that it appears emphasis is placed on the lending policy rate.

Despite the significant rise in commodity prices, global inflation remains well contained. This was attributed partly to the decline in the real value of the US Dollar, but mainly to the proactive policy stance by central banks.

The Committee underscored that the Gambia's terms of trade has deteriorated thanks to higher oil prices and a decline in the prices of groundnut and groundnut products, the country's main domestic exports. The appreciation of the real effective exchange rate of the Dalasi may have also dented the Gambia's competitiveness.

(2.0) Balance of Payments (BOP) Developments

Preliminary projections indicate an overall BOP surplus of D240.0 million ($8.0 million), lower than D320.9 million ($11.2 million) in 2005. This mainly reflected projected decline in the capital account surplus and a worsening of the current account deficit. Gross external reserves estimated at US $99.2 million in 2006, up from $93.7 million in 2005 and adequate to cover 4.5 months of imports.

The trade balance is projected at a deficit of D3.0 billion compared to D2.9 billion in 2005 largely reflecting higher oil-related imports. Imports are projected to increase to D7.0 billion, or 10.1 per cent. About 70.6 per cent of imports are classified as imports for domestic consumption and the balance for re-exports. The value of oil imports is estimated at D1.4 billion ($46.6 million), compared to $40.3 million and $29.5 million in 2005 and 2004 respectively. Exports are projected at D4.0 billion compared to D3.6 billion in 2005. Groundnut exports should total D435.0 million ($14.5 million) against D325.6 million ($11.3 million) in 2005.

Travel income is projected to increase to D2.6 billion ($85.6 million), or 19.3 per cent owing to the estimated 12.0 per cent increase in tourist arrivals. Reflecting the increase in the external debt stock, net interest payments is expected to rise to D1.5 billion ($51.5 million) compared to D1.3 billion ($45.5 million) in 2005.

Private remittances, which broadly include unrequited transfers from migrant workers, are a major source of foreign exchange for the Gambian economy. `Remittances are projected at D1.0 billion ($34.1 million) in 2006 compared to D856.3 million ($29.8 million) in 2005. Private unrequited transfers should amount to D129.0 million relative to D117.3 million in the preceding year.

The current account deficit, excluding official transfers, is projected to worsen to D2.6 billion in 2006. Including official transfers, the current account deficit is projected at D1.7 billion, same as in 2005.

The capital account is estimated at a reduced surplus of D2.0 billion, or 2.9 percent from 2005. Net official loans is projected at D510.0 million relative to D489.2 million in the previous year, reflecting higher inflows from projectrelated loans estimated at D1.2 billion, over and above the D911.4 million in 2005. Foreign direct investment (net) is projected to increase by only 1.0 percent to D1.3 billion. Tourism continues to attract the bulk of the FDI inflows.

The Committee doubted the veracity of the remittances data obtained from the banks and foreign exchange bureaux as part of a separate exercise to migrate from BPM4 to BPM5. The under reporting was attributed to classification problems. The Committee re-emphasised the importance of remittances and urged that greater effort be put into compiling this major source of foreign exchange from source. The argument was made that transfers through Western Union could form a good basis for estimating remittances.

(3.0) Developments in the Foreign Exchange Market

The Dalasi remains firm against most major currencies. In March 2006, the Dalasi appreciated by 3.6 percent, 9.3 percent and 9.6 against the US Dollar, Pound Sterling and Euro from a year ago. Fundamental factors such as increased FDI, tourism and re-exports related flows continued to support the Dalasi.

Volume of transactions, that is, total purchases and sales in interbank foreign exchange market increased to D7.6 billion in Q1, 2006, higher than D6.7 billion in Q4, 2005.

The US Dollar depreciated against most of the major currencies in the international foreign currency markets in Q1, 2006 after a brief appreciation in early 2006. Although economic growth in the US remains strong, the large current account and budget deficits were deemed to be main reasons for the Dollar's weakness against the Pound Sterling rather than improved macroeconomic fundamentals in the UK. In contrast, the Euro's appreciation mainly reflected positive developments in a number of Euro zone countries, including Germany.

(4.0) Fiscal Developments

Preliminary data indicate that Government's domestic revenue performance improved significantly in Q1, 2006 compared to Q1, 2005. However, the outturn was below the budget projection by D33.4 million, or 4.2 percent.

Expenditure and net lending totalled D565.7 million relative to D1.25 billion in Q1, 2005. The outturn was also significantly below the budget projection of D795.1 million.

The Basic balance, defined as domestic revenue minus expenditure and net lending excluding externally financed capital expenditure, was in a surplus of D200.8 million, over and above the Staff Monitored Programme (SMP) target of D88.6 million but below the budget figure of D431.0 million.

The Committee commended the authorities for meeting all the fiscal targets under the SMP, but urged that the fiscal consolidation process be sustained. A lower domestic borrowing should lead to a reduction in interest rates thereby providing the fiscal space for increased spending in the social sectors, such as health and education.

(5.0) Money Market Developments.

As at end- March 2006, the stock of interest bearing debt rose to D5.1 billion, or 4.8 percent from a year ago. However, relative to end-December 2005, the stock decreased by 3.0 percent.

Deposit money banks held the bulk of debt (41.5 percent) followed by the non-bank public including parastatals (39.2 percent) and Central Bank of the Gambia (19.3 percent).

The shift from shorter to longer-dated Treasury Bills was quite pronounced in March 2006. One (1) year bills accounted for 73.0 of the stock of outstanding bills, 182-day bills (21.0 percent) and 91-day bills (6.0 percent). In December 2005, 1-year bills accounted for 64.0 percent of the stock, 182-day bills (21.9 percent) and 91-day bills (14.1 percent).

There was a discernible decrease in the participation of parastatals in the Treasury bills market. Correspondingly, deposit money banks' holdings of Treasury bills increased. It was the view of the Committee that this development may crowd out private sector credit. Private sector credit grew by 21.2 percent in 2005, albeit from a low base and early indications are that the growth rate would be lower in 2006.

The Committee noted that the recently introduced primary dealership system is functioning smoothly. And, given that those licensed as primary dealers have a better understanding of the market, may lead to a more stable interest rates structure.

(6.0) Monetary Developments

Money supply grew by 12.0 per cent in the year to end-March 2006 compared to 24.0 percent a year earlier. However, the growth rate in money supply was slightly higher than the end-March 2006 programmed target of 11.5 percent. Both components of money supply increased but quasi money grew at a faster pace (21.6 percent) than narrow money (5.0 percent) probably reflecting portfolio shift to higher yielding assets in an environment of macroeconomic stability.

Regarding the factors affecting money supply, the net foreign assets (NFA) of the banking system declined slightly to D3.3 billion, or 1.2 per cent. This was mainly on account of the decline in the NFA of the deposit money banks to D1.3 billion, or 3.7 percent. Although foreign liabilities fell by 87.2 percent, this was offset by 10.2 percent decrease in foreign assets. In contrast, the NFA of the Central Bank rose slightly to D2.1 billion, or 0.4 percent. Gross official reserves fell to D2.7 billion, or 3.3 percent while foreign liabilities decreased to D609.3 million, or 14.0 percent.

The net domestic assets (NDA) of the banking system rose to D3.2 billion, or 30.3 percent. This was as a result of 28.2 percent and 19.0 percent increase in domestic credit and other items (net) respectively. Credit to private sector rose to D2.1 billion, or 21.2 percent. Claims on public entities and net claims on Government also increased by 31.6 percent and 38.6 percent to D256.4 million and D1.5 billion respectively.

Reserve money, the Bank's operating target, grew by 9.6 percent, lower than the growth rate of 15.6 percent a year earlier. However, reserve money growth was slightly higher than the end-December programmed target of 7.7 percent. Under the SMP, targets are set for net usable reserves (NUR) and net domestic assets (NDA) of the Central Bank. Net usable reserves was above the target (floor) by D29.9 million while the NDA was below target (ceiling) by D104.7 million.

The Committee observed that growth in reserve money above target was attributed to the fact that purchases of foreign exchange to build up foreign reserves were not fully sterilized.

Commenting on the usefulness of broad money measures as indicators of aggregate nominal spending, the view was that it depends on the predictability of the relationship between nominal expenditure and the stock of broad money. Broad money growth outpaced growth in nominal GDP in 2005, causing money velocity to decline. A decrease in velocity is normally associated with deceleration in inflationary pressures.

The observation was also made that looking at the sources of the monetary base, net credit to Government had a contractionary impact on reserve money by almost the same magnitude as in 2004. In essence, monetary and fiscal policy mix appeared appropriate in both 2004 and 2005.

(7.0) Financial Stability Report

According to the report, as at the deadline of March 2006 all 7 commercial banks observed the minimum paid-up capital requirement of D60.0 million that was introduced in 2004. A capital verification exercise was conducted on all the banks to ensure that all the accounting entries were appropriately passed.

The banking industry's aggregate assets, deposits, capital and reserves and net earnings rose in Q1, 2006 relative to Q4, 2005. On the down side, the ratio of non-performing loans to total loans and advances increased.

Total deposits increased from D4.72 billion in Q4, 2005 to D4.95 billion in Q1, 2006. Two banks accounted for 75.0 percent of total deposits, indicating a high degree of market concentration.

Aggregate assets rose to D8.2 billion, or 18.6 percent. Loans and advances accounted for 26.2 percent of total assets. Two banks accounted for 72.1 percent of total industry assets.

Net earnings surged to D71.0 million, or 26.9 percent. This mainly reflected increased interest income and a decline in interest expense. Interest income rose by 9.0 percent while interest expense recorded stagnant growth.

The industry's average capital adequacy ratio was 62.4 percent. All the banks observed the minimum ratio of 8.0 percent. The highest ratio was 219.1 percent and the lowest (15.6 percent).

Although non-performing loans (NPL) decreased to D234.6 million, or 1.5 percent from Q4, 2005, the ratio of non-performing loans to loans and advance was 12.1 percent, over and above the recommended 10.0 percent.

The banking industry is highly liquid. The liquidity ratio of the industry rose to 142.1 percent in Q1, 2006 compared to 131.3 percent in Q4, 2005. The lowest ratio was 63.4 percent, significantly higher than the statutory required ratio of 30.0 percent of deposit liabilities.

The Committee expressed concern about the size of the non-performing loans, notwithstanding the fact that they were adequately provisioned. It was averred that a good chunk of the non-performing loans was on account of a default by a major player involved in groundnut marketing.

On the concerns raised by the Bankers' Association regarding certain provisions of the FIA 2003, the Committee agreed on the need to carry out a comprehensive review of the Act to ensure that the legal framework is supportive of financial sector development.

(8.0) Real Sector Developments

Growth in gross domestic product (GDP) was estimated at 6.9 percent in 2005 compared to 6.6 percent in 2004. Agricultural output is estimated at 7.4 percent, industrial (4.7 percent) and services (7.0 percent).

Data from the Gambia Ports Authority indicated increased export volumes in Q1, 2006 totalling 21,823 metric tonnes, or 6.9 percent over Q1, 2005. However, exports data from the Gambia Civil Aviation Authority (GCAA) showed that only 451.9 metric tonnes of goods were exported via the airport, 26.4 per cent lower than the corresponding period in 2005.

Foreign currency deposits on collection basis, an indicator of the level of re-exports, totalled D2.11 billion in Q1, 2006, representing a decline of 23.2 percent over Q1, 2005.

Commenting on the report, the Committee noted that exports data from GCAA appear to be understated and that Gambia International Airlines which provides handling services to most airlines could provide a more reliable data.

On growth prospects, it was underscored that agriculture remains the linch pin of the Gambia economy. And, to the extent that above normal rainfall is forecast, coupled with continuing rebound in tourism and re-exports, and the construction boom, growth should be robust in 2006.

(9.0) Inflation

End-period inflation, measured by the consumer price index of low income population of Banjul and Kombo St Mary area, declined from 4.9 percent in March 2005 to 1.7 percent at end-March 2006. Average inflation rate (12 month moving average) was 2.2 percent compared to 11.2 percent a year earlier.

Food consumer price inflation declined to 0.7 percent compared to 5.8 percent in March 2005. Non-food consumer price inflation rose to 3.7 percent compared to 3.1 percent at end-March 2005. This was as a result of the increase in the prices of ‘‘clothing, textiles and footwear’’, and ‘’miscellaneous items'', to 2.9 percent, and 5.0 percent compared to 1.2 percent and 2.2 percent in March 2005.

Core inflation, which excludes prices of energy and volatile food items, decelerated from 2.7 percent in March 2005 to 1.5 percent in March 2006. The decrease in inflation was achieved under conditions of accelerating economic growth and rising incomes.

Prudent monetary policy in general and the broadly stable Dalasi exchange rate in particular had a favourable impact on prices of imported goods. This, in turn, dampened inflationary expectations and exerted pressure on firms to contain prices of domestically produced goods.

(10.0) Inflation

The outlook for inflation is good, despite high and volatile oil prices. Headline and underlying inflation should remain subdued in the near term owing to the following:

(i) Despite strong global growth and high and volatile oil prices, global inflationary pressures remain modest. While headline inflation has picked up in response to higher oil prices, core inflation remains contained and inflationary expectations well grounded;

(ii) The Dalasi exchange rate is expected to be stable underpinned by inflows from remittances, transfers and foreign direct investment;

(iii) Growth in the monetary aggregates would be modest and in line with projections.

(11.0) Monetary Conditions Index (MCI)

The MCI provides the policy maker with the flexibility to make smaller changes to one variable and make compensatory changes to the other as sometimes required by market conditions. This flexibility is more useful when exchange rates are freely floating without much intervention by the monetary authority. The MCI, in effect, is a simplified numeral indicator of the relative “tightness” or “looseness” of monetary policy. It captures in a single number the degree of pressure that monetary policy is exerting on the economy and, therefore, on inflation and growth.

When a central bank makes a change to the monetary instruments with the objective of having an impact on the final targets, the inflation rate and the growth rate of the economy, the transmission could take place through several channels. Interest rates and exchange rates are the two main channels through which the effects of changes in monetary policy are transmitted to the final targets. Therefore, interest rates and exchange rates could serve as operational targets and could be used to guide monetary policy.

The Central Bank’s MCI assigned a weight of 1.0 for interest rates and 2.4 for exchange rates. The MCI indicated that after 9 months of persistent easing, monetary conditions tightened slightly in March 2006. The end- March 2006 reading was 0.1 compared to negative 3.4 in February 2006 reflecting in the main marked increase in real interest rates.

(12.0) Against this backdrop and in light of the latest inflation projection, the MPC decided to reduce the rediscount rate, the policy rate, by 2.0 percentage points to 15.0 percent. The MPC would continue to monitor the situation and if the outlook changes, the Committee would review its stance.