MINUTES OF THE MONETARY POLICY COMMITTEE MEETING

August 30-31, 2007

The twentieth meeting of the Monetary Policy Committee (MPC) of the Central Bank of The Gambia was held in the Conference Room of the Bank on August 30, 2007.

Present were:

Momodou B. Saho	-	Governor, Chairman
Basiru A. O. Njai	-	First Deputy Governor, Member
Oumie Savage Samba	-	Second Deputy Governor, Member
Ousman Sowe	-	Director, Financial Supervision Dept., Member
Amadou Colley	-	Director, Banking Department, Member
Buah Saidy	-	Director, Economic Research Dept, Member
Ada Gaye	-	Deputy Permanent Secretary, DOSFEA
Amie Khan	-	Economist, DOSFEA
Bakary Kolley	-	Principal Economist, Economic Research Dept (Secretary)

In Attendance Were:

Omar Jaata	-	Director, Foreign Department
S. Bai Senghor	-	Director, Micro Finance Department
Essa Drammeh	-	Deputy Director, Financial Supervision Dept.
Paul Mendy	-	Deputy Director, Financial Supervision Dept.
Alieu B. S. Gaye	-	Deputy Director, Risk management Unit
Omar Janneh	-	Principal Personnel Officer, Admin. Dept
Mbaye Jammeh	-	Principal Officer, Banking Department
Ebrima A.C. Ndong	-	Principal Officer, Foreign Department
Seeku Jaabi	-	Principal Officer, Micro Finance Dept.
Abdoulie Jarra	-	Senior Economist, ERD
Bakary Jammeh	-	Senior Econometrician, ERD
Buba Touray	-	Senior Economist, ERD

Nyakassi Sanyang	-	Statistician, ERD
Lamin Jarjue	-	Banking Officer, BD
Mustapha Samateh	-	Banking Officer, FSD
Isatou Mendy	-	Economist, ERD
Abdoulie Touray	-	Banking Officer, FSD
Alagie Darboe	-	Banking Officer, FSD
Alagie Sowe	-	Banking Officer, FSD
Paul Solomon Bruce	-	Assistant Statistician, ERD

Before turning to its immediate policy decision, members of the MPC discussed and adopted the minutes of the previous meeting with few amendments. This was followed by presentations on international developments, balance of payments (BOP), foreign exchange, monetary developments, money market, financial stability, real sector, government fiscal operations and inflation.

(1.0) Developments in the International Economy

The global economy continues to expand. Output growth is projected at 5.2 per cent in 2007 and 2008 owing in the main to increased economic activity in emerging economies, particularly China, India and Russia. Africa, as a whole, is expected to grow at a robust pace of 6.4 per cent in 2007, reflecting rising mining and hydrocarbon production as well as improved macroeconomic conditions. Economic growth in Africa is expected to be even higher in 2008, with output projected to grow by 6.9 per cent.

Growth in the United States is projected at 2.0 percent in 2007, albeit 0.2 percentage points lower than the earlier projection. Economic activity is expected to rebound somewhat and return to potential by mid 2008.

In the Euro area, GDP grew by 2.8 percent in 2006, the strongest growth performance in six years. However, a number of factors are likely to slow growth in 2007 including economic slow down in the US and the appreciation of the Euro against the Dollar. Overall, economic growth in the Euro zone is expected to be close to potential over the next few years, despite the near term effects of current financial conditions.

The Japanese economy is expected to grow by 2.6 percent in 2007 from 2.2 percent in 2006. Domestic demand rebounded after a slow down in the middle of 2006 moving the economy out of the deflationary spiral.

In the UK, growth was weaker-than-expected in the second quarter of 2007 and was estimated at 0.8 per cent. Recent floods and financial events are expected to slow growth in the second half of 2007.

Inflationary pressures generally abated despite strong global growth. However, some emerging market and developing countries have started to experience rising inflation, especially from energy and food prices.

Commodity prices declined in August 2007 due to decreased global demand attributable to the US sub prime market debacle and lower-than-expected growth in the US, the largest economy in the world. Oil prices fell to below US $69.0 for the first time since June 2007. The price of gold, coffee and sugar also declined.

The Committee observed that even though global growth is robust, inflation remains relatively low owing in large part to the proactive stance of central banks in putting a lid on inflation as well as on-going structural reforms. And given that inflationary pressures show signs of a build up, expectations are that the tightening cycle of central banks would continue, at least in the near term.

The Committee noted that the most effective way of reducing poverty is through broad based economic growth. And to the extent that global growth is solid and inflation subdued, global poverty should decline. Regarding developments in the sub prime market, the Committee concurred that though financial market conditions have improved somewhat over the past few days, the market is still fragile and that further adverse credit market developments could well increase the downside risks to the global economy. The US sub prime debacle should however have minimal effect on the domestic financial market given that financial institutions in The Gambia rely on domestic resources and less on external sources of funding, e.g the international money market.

(2.0) Balance Of Payments (BOP) Developments

The overall balance of payments is projected at a surplus of US$30.3 million in 2007 compared to US$27.1 million in 2006. The current account balance including official transfers is expected to narrow to D830.0 million compared to D1.28 billion in 2006 premised on strong exports, including re-exports, increased travel and communications income and decline in interest payments assuming The Gambia obtains debt relief in 2007. The capital and financial account balance is projected to decline to D1.69 billion from D2.04 billion in 2006, reflecting decreased external borrowing.

Balance of payments data for the first quarter of 2007 indicate an overall deficit of D59.2 million. The current account deficit, including official transfers is estimated at D58.7 million and the capital and financial account deficit at D0.54 million.

The Committee noted that it would be useful to express the current account deficit as a percentage of GDP and also to provide the data in a historical context. The communications services balance should also be revisited given that the first quarter estimated balance was only D1.62 million which is significantly dwarfed by the projection of D305 million for the entire 2007.

(3.0) Foreign Exchange Developments

The inter-bank foreign exchange market continues to deepen. Transaction volumes, measured by aggregate purchases and sales, rose to D24.8 billion in the seven months to end-July 2007, or 35.0 per cent from the corresponding period in 2006.

Reflecting improved macroeconomic fundamentals, the dalasi strengthened against all major currencies traded in the domestic inter-bank market. Between December 2006 and July 2007, the Dalasi appreciated by 3.8 per cent, 9.7 per cent, 2.2 per cent and 4.9 per cent against the Pound Sterling, U.S. Dollar, Euro and CFA franc respectively.

Looking forward, the appreciation of the Dalasi is expected to continue in the near term supported by increased foreign inflows from foreign direct investment, privatization receipts, private remittances, increasing receipts from tourism, cashew and mineral sands exports, as well as healthy reserves and implementation of prudent fiscal and monetary policies which have restored confidence in the Gambian economy.

Given that the primary remit of the Central Bank is price stability, the appreciation of the Dalasi should help in achieving the inflation target. Prices of consumer goods could be much lower if competitive pressures induce a greater pass-through of the exchange rate appreciation. However, putting the wider economy into perspective, an appreciation of the real effective exchange rate may hurt exports, including exports of services. In essence, while the growth in imports is expected to be robust, the growth of exports may weaken owing to the higher level of the Gambian Dalasi. The Committee observed that to make an informed judgement more rigorous research is needed, particularly in the area of equilibrium exchange rate. In addition, a real effective exchange rate index should be introduced rather than relying on anecdotal evidence.

(4.0) Government Fiscal Operations

The public finances performed better-than-projected in the first half of 2007. Domestic revenue exceeded projection by a substantial D204.0 million on the back of increased tax and non-tax revenue. Total expenditure and net lending, on the other hand, was below target (ceiling) by about D560.0 million.

The overall fiscal balance (on cash basis) recorded a surplus of D415.3 million compared to a projected deficit of D96.7 million.

The basic balance, that is, domestic revenue less total expenditure and net lending, excluding externally financed capital expenditure was 3.2 per cent of GDP, double the target set under the PRGF program with the Fund. The basic primary balance was 6.0 per cent of GDP which if sustained, should put a damper on the domestic debt.

The Committee welcomed the prudence on the part of the fiscal authorities which should help the Central Bank achieve its inflation target. However, looking forward, the appreciation of the Dalasi may lead to a decrease in domestic revenue from international trade which if not matched by a reduction in expenditure may lead to a wider-than-projected budget deficit. On the other hand, government and private sector foreign debt service payments could be positively impacted given that the appreciation of the Dalasi would lower debt service payments in domestic currency.

(5.0) Money Market Developments

Money market developments were characterised by a marginal increase in the interest bearing debt to D5.1 billion, or 1.4 per cent from end-December 2006, a shift in the distribution by holder and a declining trend of the discount rate at least over the past two months. The decline in the discount rate was attributed to increased competition, reflecting the high demand for Dalasi assets in light of the appreciation of the domestic currency, coupled with decreased supply owing to the improved fiscal position of Government. The commercial banks held the bulk of the interest bearing debt (58.1 per cent), the non-bank public (37.4 per cent) and the Central Bank of The Gambia (4.5 per cent).

The Committee welcomed arrangements by the Central Bank of The Gambia and Department of State for Finance and Economic Affairs to sign a Memorandum of Understanding (MoU) in the area of domestic debt management and monetary operations. The MoU would succinctly spell the roles and responsibilities of each institution and the coordination mechanism with a view to ensuring that the fiscal/monetary policy mix is right.

Members noted the increase in inter-bank placements which should enhance the allocation of credit and the monetary policy transmission mechanism. Although the inter-bank market is quite shallow, the volume of transactions totalled D439.0 million between September 2006 and August 2007. Virtually all the banks participated actively in the market. The Central Bank is at an advanced stage of introducing repos which is expected to facilitate collateralized lending and help deepen the market.

(6.0) Monetary Developments

Monetary policy in 2007 is aimed at achieving the inflation target of 5.0 per cent by end-December 2007. Money supply grew by 17.2 per cent in the year to end-July 2007 compared to 16.3 per cent a year earlier. Narrow money increased by 15.1 per cent and quasi money by 19.4 per cent. Money supply grew by only 2.3 per cent from the beginning of the year.

Reserve money, the bank’s operating target, grew by 6.6 per cent, lower than the 16.2 per cent a year earlier. Compared to end-December 2006, reserve money growth was a negative 10.5 per cent.

Expectations are that money supply and reserve money would grow below the end-December targets of 13.3 per cent and 10.6 per cent, respectively reinforcing expectations of deceleration in inflationary pressures. Given that reserve money growth was negative relative to end-December 2006 and actual reserve money was below target by D25.11 million on August 23, 2007, coupled with the marked appreciation of the Dalasi the Committee generally agreed of the need to inject Dalasi liquidity preferably by the Central Bank purchasing foreign currency.

(7.0) Financial Stability Report

The banking sector remains sound. The capital adequacy ratio was 26.1 per cent at end-June 2007, higher than the minimum requirement of 8.0 per cent.

Total assets rose to D9.89 million, or 17.3 per cent from end-June 2006. Gross loans and advances totalled D2.29 billion, but lower than D2.35 billion in June 2006, reflecting tightening of credit conditions to rein in non-performing loans. Non-performing loans to gross loans was 13.0 per cent in June 2007, higher than 12.6 per cent in March 2007.

Deposit liabilities increased to D6.19 billion, or 14.6 per cent from a year ago, reflecting rising income and vigorous savings mobilisation drive in light of increased competition.

The Committee observed the precipitous decrease in the profitability of banks in the second quarter of 2007 compared to the same period last year, which was attributable to a number of factors, including decrease in private sector credit, the marked decline in treasury bills yields, increased interest and non-interest expense and decline in non-interest income. Despite the decreased profit, the banking sector return on assets (ROA) of 1.82 per cent was considered commendable. Members noted the deceleration in private sector credit and concurred that tighter credit conditions may weigh particularly on investment and other components of aggregate demand in the coming quarters and could down economic activity.

(8.0) Real Sector Developments

The GDP growth forecast of 7.0 per cent is unchanged. The upside risks to growth increased somewhat, underpinned by plentiful and well distributed rainfall which should increase agricultural production, expanding services sector, including banking and tourism and the continuing boom in the construction and communication sectors.

Recent data and anecdotal information indicate diversification within the agricultural sector away from groundnuts in particular to food crops, owing in large part to the difficulties experienced by farmers in marketing groundnuts over the past years. The Committee welcomed the positive developments in the agricultural sector and noted that the key to reducing rural poverty is to significantly scale up agricultural production and productivity. This, in turn, implies investing in appropriate technology and extension services as well as ensuring that farmers have access to vital inputs.

(9.0) Inflation

End-period inflation, measured by the National Consumer Price Index (NCPI), rose from 1.5 per cent in July 2006 to 6.3 per cent at end-July 2007. The average inflation rate was 3.2 per cent compared to 3.1 per cent a year earlier. The main driver of inflation was food prices which rose to 9.7 per cent compared to 1.1 per cent in July 2006.

Non-food prices rose by a modest 2.5 per cent from 2.1 per cent in July 2006. Core inflation, excluding prices of energy and utilities as well as volatile food items increased from 1.8 per cent in July 2006 to 6.3 per cent in July 2007.

The consumer price inflation of non-alcoholic beverages rose to 1.9 per cent from 1.5 per cent in July 2006. Owing to the significant rise in the food consumer price inflation, the combined food and non-alcoholic beverages inflation accelerated to 9.5 per cent.

Non-food and services consumer price inflation rose to 2.5 per cent from 2.1 per cent at end-July 2006 as a result of deceleration in the prices of “alcoholic beverages”, “tobacco and narcotic”, “furnishings, household equipment, etc”, “clothing, textiles and footwear”, “hotels, cafes and restaurants”, “miscellaneous good and services”, “health”, “communications”, “transport”, and “recreation and culture” to 1.5 per cent, 4.4 per cent, 2.2 per cent, 2.0 per cent, 3.5 per cent, 8.2 per cent, and 0.2 per cent compared to 1.4 per cent, 2.2 per cent, 1.7 per cent, 1.6 per cent, negative 3.3 per cent, 1.2 per cent, and negative 0.3 per cent respectively.

Core measures of inflation attempt to strip out the effects of temporary disturbances (noise) from headline inflation in order to uncover underlying inflation. The so-called noise in headline inflation was striped-out by excluding prices of energy and utilities (fuel, light and transport) and volatile food items.

The first measure of core inflation (Core 1), which excludes energy prices (housing, water, electricity, gas, other fuels and transportation) rose from 0.9 per cent in July 2006 to 6.2 per cent in July, 2007.

Core 2, which excludes prices of “energy and utilities and volatile food items” “meat”, “fish’’, “bread and cereals”, ‘‘ alcoholic beverages and tobacco”, and ” milk, cheese and eggs‘‘ increased from 1.8 per cent in July 2006 to 6.4 per cent at end-July, 2007.

Members observed that readings of current inflation figures have not demonstrated a sustainable moderation of inflationary pressures notwithstanding the appreciation of the dalasi, miniscule growth in money supply and supportive fiscal policies over the past seven months. The Committee made no revisions to the near term outlook for inflation convinced that the downside risks to inflation, driven by the marked appreciation of the Dalasi, outweigh the upside risks.

(10.0) Decision

Taking the above-mentioned factors into consideration, including the risks to the inflation outlook, the Monetary Policy Committee (MPC) decided to maintain the rediscount rate, the policy rate, at 15.0 per cent. The MPC would continue to monitor changes in economic conditions and respond appropriately in discharging its mandate to maintain price stability.