MINUTES OF THE MONETARY POLICY COMMITTEE MEETING

The second meeting of the Monetary Policy Committee was held on October 14, 2004 at the Conference Room of the Central Bank. The following members of the Committee were present.

- Famara L. Jatta - Governor, (Chairman)
- Momodou B. Saho - Member
- Ousman Sowe - Member
- Basiru Njai - Member
- Amadou Colley - Member
- Mod Secka - DoSFEA, Member
- Buah Saidy - Secretary

Absent

- Teneng Jaiteh - DoSFEA, Member

Observers

- Oumie Savage-Samba - Ag. Director, Finance and Infor. Systems Dept.
- Pa Alieu Sillah - Deputy Director
- Omar Jatta - Ag. Deputy Director, FED
- Philip Akibogum - Principal Officer, FED
- Mbye Jammeh - Principal Banking Officer, BSD
- Lasana Fati - Principal Auditor, IAD
- Essa Drammeh - Principal Officer, FSD
- Abdoulie Jarra - Senior Economist, ERD
- Momodou Sabally - Economist/Statistician, ERD
- Ismaila Jarju - Economist, ERD
- Ida Fye - Banking Officer, FSD
- Karamo Jawara - Banking Officer, BSD
- Bakary Jammeh - Econometrician, ERD

- Maimuna John-Sowe - Economist, ERD

Before reaching a policy decision and against the backdrop of the forward looking business sentiment survey and the latest projections for inflation, the Committee discussed developments in the world economy, balance of payments, foreign exchange, fiscal sector, money market, money and credit and the real sector.

Global Economic Outlook

During the ensuing discussions, the inflation figures of some African countries were questioned but some of the Committee members were of the view that the numbers were correct. Concern was raised about the worrying high inflation in Guinea and it was noted that Guinea’s economy was saddled with difficulties thanks in large part to expansionary monetary and fiscal policies. However, the expectation was that the current economic adjustments being resolutely implemented by the Guinean authorities should put a damper on inflation in due course.

Ivory Coast and Guinea Bissau where singled out as low inflation countries inspite of the seemingly intractable political crises besetting the two countries. It was explained that the two countries’ membership to the CFA zone was principally responsible for the minuscule rates of inflation. To the extent that the CFA appreciated in tandem with the Euro, its anchor currency, it impacted positively on prices.

Regarding the availability of rice in the world market and the impact the rising price of the commodity is having on the Gambia, the Committee observed that the domestic price of rice has been stable for sometime attributed to the stability of the Dalasi and increased supply of the commodity thanks to the Italian and Japanese rice grants. Given the stability of the Dalasi and the projected increase in domestic rice production, the expectation is that the price of rice would remain stable at least in the near term.

On the issue of terms of trade data, it was noted that although the Department of State for Finance and Economic Affairs should be responsible for its computation, the data is not always readily available. The Economic Research Department would nonetheless endeavour to do the computation subject to data availability. Notwithstanding, it was felt that the Gambia's terms of trade remains favourable given the increase in the prices of our major exports.

The Committee also took note of the rising trend in freight and insurance costs attributed partly to the increase in oil prices and partly to the marked growth in international trade.

The Committee observed that the European Central Bank (ECB) continues its accommodating stance despite the increase in oil prices and the fact that the US has started to use its oil reserves to stabilize domestic fuel prices. The point was also made that according to industry analysts, the price of oil should hover around US$30.0 – 36.0 per barrel given the level of supply and demand. Therefore, to the extent that prices have exceeded US$50.0 mainly reflect a high risk and speculation premium.

External Sector Developments

It was observed that there is an urgent need to improve the Gambia's trade balance by increasing exports. In particular, high value fish and horticultural exports should be encouraged given their potentialities. The Committee was also of the view that taking into account the fact that The Gambia enjoys a comparative advantage in tourism and to some extent re-exports, it is equally important that these two sectors are vigorously promoted.

Members pointed out that it is important to report imports of capital and intermediate goods separately because of their potential to predict economic activity. The projected 2004 current account deficit was deemed not particularly worrying given that it would be financed fully by foreign direct investment (FDI) inflows.

The Committee also underscored the need to improve BOP statistics especially private transfers data which is believed to be grossly understated. It was observed that ERD is working with FSD to obtain monthly data on private remittances from banks and foreign exchange bureaux. The proposed second phase of foreign private capital flows project slated for actualization in 2005 should also help to improve the BOP estimates.

Deliberating on the foreign exchange market, the Committee lamented the continuing depreciation of the Dalasi against the CFA. However, it was pointed out that it is difficult to obtain reliable statistics on the CFA because the banks do not actively trade the currency. It was opined that the Dalasi is expected to be stable against the CFA by year end premised on growth in re-exports, particularly to neighboring CFA zone countries.

Fiscal Developments

The Committee expressed delight in the improved performance of the fiscal sector, but was concerned that taxes on international trade fell below projection. However, the data on international trade was deemed inaccurate and the ERD was tasked to review and validate the data.

The Committee raised concern about the slow pace of the land sales and expressed the hope that the process will be accelerated so that the fiscal targets agreed under the Staff Monitored Programme (SMP) would be realised.

Money Market Developments

The Committee noted with concern the mounting domestic debt and suggested that the debt be restructured by, *inter alia*, transforming some of the debt into long-term bonds, say, three-year bonds. However, a better and lasting solution is to substantially increase the primary balance as well as use privatization proceeds to pay down the debt. But more fundamentally, maintaining the debt at a sustainable level requires reining in the budget deficit.

It was observed that the balance in the Special Deposit Treasury Bills Account has improved markedly thanks to the sterilization of proceeds, but the Treasury main account has been stubbornly in the red despite the increase in Government revenue.

Regarding financing of the budget deficit, it was observed that all the four modes of financing are associated with macroeconomic imbalances. External financing causes an increase in the foreign debt while domestic bank financing crowds out the private sector. Central bank financing or monetisation is inflationary and non-bank financing puts upward pressure on interest rates. The budget deficit has been largely financed by the non-bank because it is deemed a lesser of the four evils.

Monetary Developments

The Committee hailed the implementation of a prudent mix of monetary and fiscal policies, which has resulted in a marked deceleration in the growth rate of reserve money and money supply, and the concomitant containment of inflationary pressures and a stable exchange rate. The Committee observed the substantial year-on-year decline in private sector credit in the third quarter, which was attributed to the high interest rates and the seasonal decline in economic activity.

Financial Stability Report

The Committee lamented the high level of non-performing loans attributed to high interest rates, increasing competition amongst banks and possibly the absence of a credit bureau where banks can share information on borrowers. It was observed that the absence of a credit bureau should not deter the sharing of information if banks explicitly state in their policies that they would share the credit history of their customers with other banks.

On the issue of banks' profits, it was pointed out that the Financial Stability Report should dwell in more detail on profitability ratios such as return on equity, return on assets, etc. Overall, it was observed that banks are quite sound and profitable.

Real Sector

Owing to the fact that agriculture, the dominant sector of the economy, is at the mercy of the weather, growth in gross domestic product (GDP) is highly volatile. Therefore, ensuring that agriculture is less rainfall dependent would enhance economic growth as well as reduce volatility. The Committee welcomed the proposal to establish a composite index of economic activity which should enable the Bank better predict output growth by observing the behavior of a number indicators with predictive potentialities. It was also observed that if the index is successfully implemented, The Gambia would join the ranks of few African countries that have use such an index.

On the performance of re-exports, it was noted that once the tariff harmonization exercise is fully implemented in the sub-region, The Gambia's competitive edge would be eroded unless there are sufficient efficiency gains. It was also emphasized that far-reaching structural reforms are needed if growth is to be sustained above the 6-7 per cent marker necessary for significant poverty reduction.

Business Sentiment Survey

Commenting on the private sector business sentiment survey, members observed that sentiments have been quite bullish particularly with regards exchange rate and inflation. There was also a strong employment expectation which could be attributed to the projected rise in sales and investment, particularly capital expenditure. The Committee found the results of the survey quite educative but moaned the poor response rate.

Inflation

On the inflation report, the Committee took note of the easing of the exchange market pressure and its attendant effect on inflation. Also, given the marked deceleration in money supply, the Committee felt that the 10.0 per cent end – December inflation target could be realized. Concern was, however, raised about the potential increase of oil prices on inflation if the US$50.0 per barrel price is sustained. An alternative view was that oil accounts for a small percentage of the consumer price index and as such its impact on consumer prices is paltry.

Regarding the increase in oil prices on Government revenue, the view was that it would have an effect unless the price increase is passed on to consumers through an upward adjustment in the retail price of oil.

Decision

The Committee observed that with agricultural production expected to increase, coupled with the concomitant stability of the Dalasi, inflation is forecast to decelerate. The Committee also took cognizance of the downside risks to the forecast.

The domestic inflation outlook is influenced not only by domestic factors but international developments as well. The strong world economic recovery is expected to be sustained and this could begin to put upward pressure on world inflation. Adding to the uncertainty of the world inflation outlook is the stronger trend in international oil prices, which is influenced not only by market conditions but by geopolitical factors as well.

Taking the above-mentioned factors into consideration, including the risks to the inflation outlook, the MPC decided to reduce the Rediscount Rate, the policy rate, by one percentage point to 33.0 per cent. The MPC would continue to monitor the situation and if the outlook changes, the Committee would review its stance.

Balance of Payments (BOP) Developments

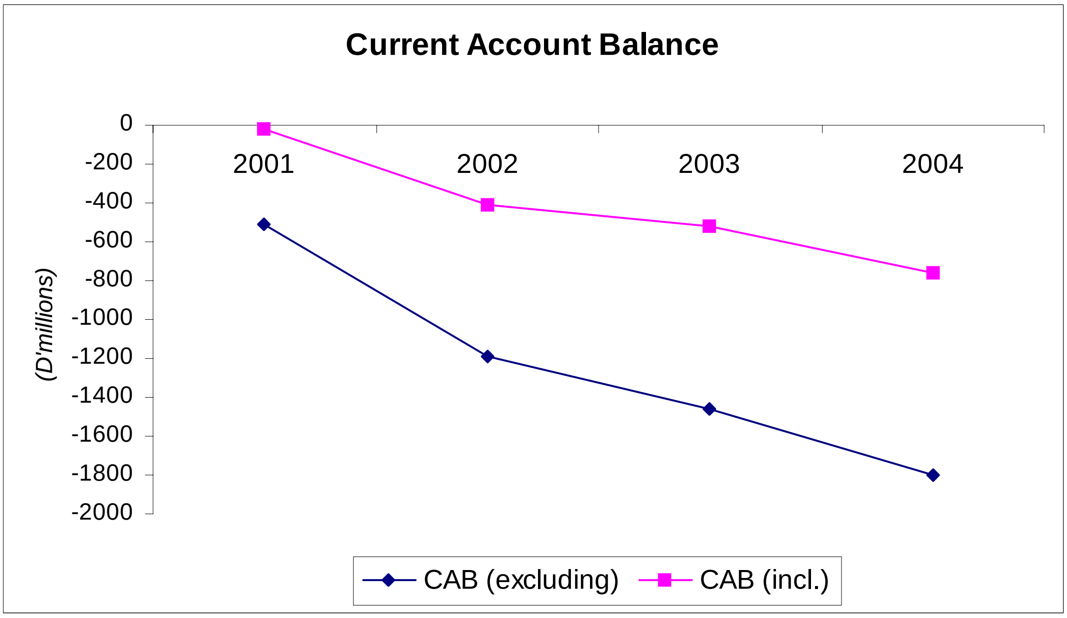
Government's external sector policy in the medium to long-term is aimed at ensuring a sustainable BOP as well as to build reserves adequate to cushion the economy against external and internal shocks. Foreign currency reserves were programmed to cover at least five months of imports in 2003 and 2004.

The balance of payments is projected to improve significantly in 2004. The overall balance is estimated at a surplus of D878.9 million in 2004 compared to a deficit of D323.4 million in 2003. The improvement should stem primarily from a substantial increase in private capital inflows, particularly FDI.

A. Current Account

The current account balance, including official transfers, is estimated at a deficit of D759.8 million compared to D517.2 million in 2003 largely as a result of the worsening of the trade balance and the deterioration in net factor services balance. Excluding official transfers, the current account is projected to deteriorate to a deficit of D1.8 billion, or 22.7 per cent.

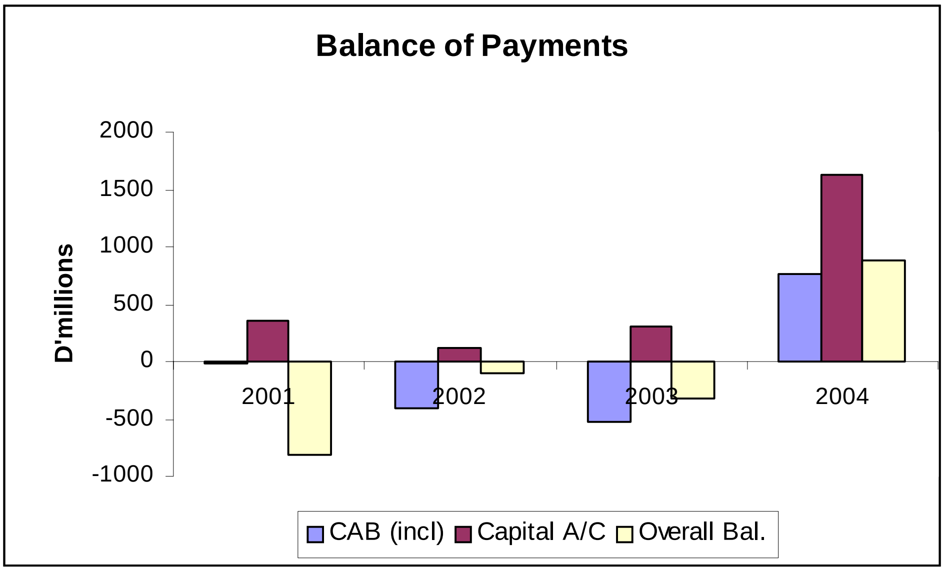
The merchandise trade balance is estimated at a deficit of D1.4 billion relative to D1.1 billion in the previous year as imports continue to grow faster than exports. The total import bill is projected at D5.2 billion, or an increase of 30.9 per cent from 2003. In terms of value, capital equipment, heavy machinery and general goods form the bulk of imports. Exports, on the other hand, are estimated at D3.9 billion compared to D2.9 billion in the preceding year. Groundnut exports were estimated at D174.3 million in 2003/04, up from D148.9 million a year earlier. Total income from tourism is projected at D1.6 billion, or an increase of 9.7 per cent from 2003.



Reflecting partly the strong growth in imports, net outflows with respect to insurance and freight costs is estimated to increase to D619.8 million, or 34.8 percent from the previous year.

The balance in the capital account, including short-term capital and errors and omissions, which recorded a surplus of D122.8 million and D299.3 million in 2002 and 2003 respectively, is projected to increase significantly to D1.6 billion in 2004 thanks to increased private capital inflows, particularly foreign direct investment (net). Foreign direct investment (net) is projected to increase to D1.5 billion, or 319.9 per cent from 2003. Tourism continues to attract most of the FDI inflows followed by the banking sector.

Reflecting these developments, the overall balance of payments is estimated at a surplus of D878.9 million in 2004 relative to a deficit of D323.4 million in 2003. As a result, gross official reserves are projected to increase by D530.0 million and repayments to the IMF amounting to D349.0 million. Exceptional financing in the form of London and Paris Club loans which amounted to D25.2 million in 2003 is projected at zero in 2004.



The Gambia Balance of Payments, 2001-2004

(D'millions)	2001	2002	2003	2004
Trade Balance	**-350.5**	**-988.8**	**-1132.8**	**-1355.2**
Exports	1600.5	2176.9	2867.1	3881.9
Imports	-19510	-3165.7	-3999.9	-5237.0
Factor Services (net)	-362.7	-445.4	-559.9	-727.2
Non-Factor Services (net)	152.9	174.7	123.2	164.5
O/w: Travel Income	751.3	951.2	1452.6	1593.4
Private unrequited transfers (net)	54.7	71.7	105.7	121.5
Official Transfers	480.8	779.9	946.6	1036.5
Current Account Balance				
Excluding official transfers	**-505.6**	**-1187.8**	**-1463.8**	**-1796.3**
Including official transfers	**-24.7**	**-407.9**	**-517.2**	**-759.8**

The Gambia Balance of Payments, 2001-2004

(D'millions)	2001	2002	2003	2004
Capital Account	**355.1**	**122.8**	**299.3**	**1634.3**
Official loans (net)	131.2	376.9	327.0	165.0
Project-related	388.5	944.0	620.4	681.6
Program loans	0.0	2.9	0.0	0.0
Amortisation	-257.3	-592.0	-293.4	-516.6
Private Capital	**223.9**	**-254.2**	**-27.8**	**1469.3**
Foreign Direct Investment (net)	159.8	180.6	360.3	1512.9
Other investments (net)	64.1	-434.7	-388.0	-43.6
o/w: Suppliers' credit	261.7	-242.8	122.2	160.0
Errors and Omissions	-693.9	176.5	-105.5	4.3
Overall Balance	**-810.7**	**-98.8**	**-323.4**	**878.9**

Financing

(D'millions)	2001	2002	2003	2004
Financing	**810.7**	**98.8**	**323.4**	**-878.9**
Change in Gross Official Reserves	687.1	17.3	298.2	-529.9
Use of IMF Resources				
Repayments	-3.7	0.0	0.0	-349.0
Disbursements	137.2	74.5	0.0	0.0
Exceptional Financing	0.0	7.0	25.2	0.0

Memorandum Items	**2001**	**2002**	**2003**	**2004**
Current Account Balance (% of GDP)				

Excluding official transfers	-7.7	-16.1	-14.6	-14.5
Including official transfers	-0.4	-5.5	-5.2	-6.1
Gross Official Reserves (end of period)				
In millions of Dalasis	1000.7	1275.0	1664.7	2465.0
In months of imports	5.4	4.2	4.4	4.9

MPC - Annex A October 2004

WORLD ECONOMY OUTLOOK

1. Economic Activity

Economic growth is expected to pick up in the world's largest economies in the second half of 2004 after a slowdown in the second quarter. Global economic growth in 2004 is projected at 5.0 per cent, its highest level in nearly 30 years. The expansion is underpinned by continued accommodative macroeconomic policies, rising corporate profitability, and wealth effects from rising equity and house prices. Although, the recovery has become increasingly broad-based geographically, some regions continue to grow more vigorously than others. In addition, the information technology (IT) revolution, presents an opportunity for sustained higher global productivity growth.

Growth in 2004 continues to be driven by the United States, with strong support from China and Japan. The euro area continues to experience a growing economic momentum, although the strength of the upturn varies across countries and in some cases, is heavily dependent on external demand.

However, risks to the recovery have increased in recent months. First, oil prices rose sharply through mid-September, driven by strong global demand and, increasingly, supply-side concerns. Considering that prices are still higher than in 2003, and with spare capacity near historical lows, the oil market remains highly vulnerable to shocks and speculative attack. Other threats included high public deficits and the relative lack of job creation during the recovery.

The growth forecast for the US was revised downwards from 4.7 per cent to 4.3 per cent whilst the projection for Japan, the euro zone and the UK were revised upwards. The six major industrialized countries (G6 – US, Japan, Germany, France, Italy and the UK) were said to have withstood the shock of a 40% rise in oil prices this year and were on course to grow by 3.5 per cent.

The growth forecast for Japan was raised from 3 per cent to 4.4 per cent. The economy was finally in a position to escape its deflationary trap as long as structural reforms continued in the financial sector. However, economists say that the country's long-term growth potential is 1-2 per cent.

Euro zone growth forecast was raised from 1.6 per cent to 2 per cent owing to expanding exports and worldwide recovery. However there are stark differences within the euro zone.

In Germany, growth in 2004 would be higher than the OECD's 1.5 per cent estimate and could reach 2 per cent. The growth has been mainly driven by rising exports – fuelled so far by the acceleration in global demand.

Growth in the UK has been slower than expected in the third quarter coupled with a surprising weakness in the labour market. The trend growth in the UK meant that there is little on no spare capacity in the economy and could lead to a build up of inflationary pressures.

Asia's developing economies, boosted by global demand for their exports, will expand faster than expected this year in spite of higher oil prices and rising interest rates (Asian Development Bank). Average gross domestic product growth in Asia, excluding Japan, would rise to a four-year high of 7 per cent this year from 6.5 per cent in 2003 (revised forecasts). The relatively strong performance in Asian could be attributed to concurrent growth in the world's major economies.

China is expected to post growth of 8.8 per cent this year, one of the fastest rates in the region, as authorities have failed to curb rising fixed investment, particularly in construction. Analysts expect China's growth to slow to 8 per cent next year. In contrast, India was likely to see growth slowing to 6.5 per cent this year and 6 per cent next year from 8.2 per cent in 2003 due mainly to high oil prices and unfavorable weather.

The outlook for Africa has improved, underpinned by greater macroeconomic stability, higher export commodity prices, lower external debt burdens through the Heavily Indebted Poor Country (HIPC) Initiative, somewhat better access to industrial country markets, a recovery in agricultural production following severe droughts in 2003 and myraid country-specific developments. The country-specific developments include increases in oil production in Angola, Chad and Equatorial Guinea. Although higher oil prices are hurting importers, the general rise in global commodity prices is projected to have a positive net impact on trade balances of many countries this year. The countries with the largest net gains are mostly oil exporters, followed by countries with substantial gains from higher prices of metal ores. For the rest of the countries, gains from higher-priced non-fuel commodities are roughly equivalent to losses from higher-priced oil imports, though a few countries face substantial net losses.

Real GDP growth in sub-Saharan Africa is projected to rise to 4.8 per cent in 2004 and 5.8 per cent in 2005. In Nigeria, real GDP is projected to slow to 4-6 per cent in 2004-05, as the boom in oil production in 2003 wanes. While windfall oil revenues are boosting the overall fiscal balance, the non-oil deficit is large and rising. South Africa's economic growth in the year to the second quarter reached 2.5 per cent, thanks to lower interest rates.

Notwithstanding, the continuing rebound in output growth, most countries are likely to fall short of achieving the Millennium Development Goals. Key challenges going forward will be to promote private investment, deepen institutional reforms, and reduce government involvement in the economy.

Table: 1 Output Projections for the "immediate" Sub-region

Real GDP (annual per cent change)	**2002**	**2003**	**2004**	**2005**
The Gambia	**3.0**	**9.4**	**7.1**	**5.0**
Guinea	4.2	1.2	2.6	3.8
Guinea Bissau	-7.2	0.6	1.0	3.4
Mali	4.3	6.0	4.5	5.6
Senegal	1.1	6.5	6.0	5.8

2. Interest Rates

With the growth in the world economy expected to remain solid, global interest rates will have to rise to put a damper on inflationary pressures. However, European Central Bank (ECB) is expected to leave interest rates unchanged at 2 per cent until a self-sustaining pickup in domestic demand is clearly underway.

In a similar move, the Bank of England's nine-member Monetary Policy Committee voted unanimously earlier this month to leave its official interest rates unchanged at 4.75 per cent but another quarter point rise is anticipated. Given signs of a cooling housing market, there is a chance of a more abrupt correction to house price inflation and the potential for an associated downward impact on consumption. The MPC has raised rates five times since last November from a low of 3.5 per cent. British interest rates are now more than double the level of those in the US and the eurozone.

The US Federal Reserve raised its key interest rates target by a quarter point on September 20, for the third time since June. The federal funds rate is now at 1.75 per cent and the FOMC perceives the downside and upside risks to the attainment of both sustainable growth and price stability for the next few quarters to be roughly equal. The federal funds rate is seen as too low to be consistent with stable inflation over time.

3. Consumer Prices

Inflationary risks remain generally moderate. Nevertheless, after falling to unusually low levels in mid-2003, inflation has turned up around the world, reflecting a combination of strong growth and higher commodity prices. Looking forward, inflationary pressures could prove stronger than expected, necessitating a sharper-than expected rise in interest rates. Monetary policy in many countries remains appropriately accommodative but the policy challenge will be to continue to manage the transition toward higher interest rates while facilitating sustained economic recovery and orderly adjustment in financial markets.

Higher oil prices had led to higher headline inflation but underlying inflation had not followed suit. In the US, inflation rose at a rate of 3.3 per cent at the end of the second quarter. However, stripping out food and energy prices, it only increased at a rate of 1.8 per cent, a slowdown from the 2.1 per cent in the first quarter.

Growth in Chinese consumer prices appears to have leveled out after rising sharply in the first half of 2004, suggesting an easing of inflationary pressures on the economy. Consumer price inflation is projected at 4.0 per cent, up from 1.2 per cent in 2003.

Eurozone inflation remained at an annual rate of 2.3 per cent, despite higher oil prices, reinforcing expectations the ECB will hold interest rates steady at 2 per cent for some time to come.

In the UK, data on the housing market suggest price growth continues to slow but this has been offset to some degree by official figures on retail spending showing a stronger than expected sales growth in August.

Japan's third quarter got off to a weak start with stagnant industrial production, rising unemployment and persistent deflation. Unemployment rose from 4.6 per cent in June to 4.8 per cent in July.

Table: 4 **Consumer Prices** (annual per cent change unless otherwise noted)

	2002	2003	2004	2005
Africa	**9.7**	**10.3**	**8.4**	**8.1**
Cote D'Ivoire	3.1	3.3	1.5	2.0
Gambia, The	8.6	17.0	12.3	6.2
Ghana	14.8	26.7	10.8	6.0
Guinea	3.0	12.9	16.6	13.8
Guinea Bissau	3.3	3.0	3.0	3.0

4. Commodity Prices

Consolidating the robust increase in commodity prices in the last quarter of 2003, the index of overall primary commodity prices increased by about 27 per cent in both US dollar and SDR terms during the first eight months of 2004. The increase is

attributable to the marked increase in energy, raw materials and metal prices reflecting a surge in global demand, particularly in Asia.

(a) Crude Oil

Developments in the oil market during 2004 were characterized by the rise in crude oil prices to record nominal highs, and higher price volatility. Average oil prices have risen substantially during the first ten months of 2004 surpassing the record set during the Iraqi invasion of Kuwait in 1990. While the decision by

OPEC in July to increase official quotas by 2 million barrels a day (mbd) and a further 0.5 mbd in August helped to lower average prices markedly to about US$33 by mid-June, subsequent tensions in oil exporting countries –particularly Iraq, Nigeria, Russia and Venezuela- pushed average prices to a new record high of US$51 on October 4, 2004.

Looking ahead, futures prices indicate that oil prices will remain high for the rest of 2004 and 2005 since both the level and growth in the global demand for oil have consistently outpaced expectations.

(b) Non-energy Commodity Prices

Following marked increase in prices in 2003, non-energy commodity prices experienced relatively modest gains during the first ten months of 2004. This follows attempts by China (a large consumer of non-energy commodities) to slow the pace of its economic expansion, and moves by the Federal Reserve to raise US interest rates.

Rice prices, after a lackluster performance in 2003, increased by 28 per cent as a disappointing harvest in China resulted to large importation. Relatively low global stocks have also supported prices.

Agricultural raw materials prices rose by 9 per cent, buoyed by growth in softwood lumber prices.

Balance of Payments

Government's external sector policy in the medium to long-term is aimed at ensuring a sustainable BOP as well as to build reserves adequate to cushion the economy against external and internal shocks. Foreign currency reserves were programmed to cover at least five months of imports in 2003 and 2004.

The balance of payments is projected to improved significantly in 2004. The overall balance is estimated at a surplus of D878.9 million in 2004 compared to deficit of D323.4 million in 2003. The improvement should stem primarily from a substantial increase in private capital inflows, particularly FDI.

A. Current Account

The current account balance, including official transfers, is estimated at a deficit of D759.8 million compared to D517.2 million in 2003 largely as a result of the worsening of the trade balance and the deterioration in net factor services balance. Excluding official transfers, the current account is projected to deteriorate to a deficit of D1.8 billion, or 22.7 per cent.

Reflecting partly the strong growth in imports, net outflows with respect to insurance and freight costs is estimated to increase to D619.8 million, or 34.8 per cent from the previous year.

The balance in the capital account, including short-term capital and errors and omissions, which recorded a surplus of D122.8 million and D299.3 million in 2002 and 2003 respectively, is projected to increase significantly to D1.6 billion in 2004 thanks to increased private capital inflows, particularly foreign direct investment (net). Foreign direct investment (net) is projected to increase to D1.5 billion, or 319.9 per cent from 2003. Tourism continues to attract most of the FDI inflows followed by the banking sector.

Reflecting these developments, the overall balance of payments is estimated at a surplus of D878.9 million in 2004 relative to a deficit of D323.4 million in 2003. As a result, gross official reserves are projected to increase by D530.0 million and repayments to the IMF amounting to D349.0 million. Exceptional financing in the form of London and Paris Club loans, which amounted to D25.2 million in 2003, is projected at zero in 2004.

3. Monetary Developments

Money Supply

Growth in money supply decelerated to 23.6 per cent at end-August 2004 compared with 40.2 per cent a year earlier. Compared with end-December 2003, money supply grew by 6.7 per cent. The substantial decrease in money supply was mainly due to the restrictive monetary policy stance of the Central Bank.

Reserve Money

Despite the vigorous use of the monetary policy instruments, reserve money grew by 25.5 percent relative to the previous year. The growth in reserve money was largely on account of the increase in NFA of the Central Bank. In contrast, the NDA of the Central Bank declined significantly by a whopping 344.4 percent.

After a modest increase in the third quarter of 2003, currency issued by the Central Bank rose sharply in the fourth quarter of 2003. This growth trajectory continued in the first quarter of 2004 before declining in the second quarter of 2004. Compared to end-June 2003, currency issued grew by 37.0 percent.

4.0 Money Market Developments

Total outstanding stock of interest bearing debt rose to 4.6 billion at end-September 2004, 31.4 per cent from a year ago. The composition of the debt as at end-September 2004 is as follows:

1. Treasury 72%
2. Development Stocks 1%
3. Discount Note Series 3%

4. Others 24%

The non-bank sector held most of the debt (45.1%) followed by the deposit money banks (34.0%).

5.0 Private Sector Business Sentiment Survey

The survey shows that sentiment on general economic and business activity has changed significantly. About 27.0 per cent of the firms are of the view that economic activity would be higher, the same as those who think it would be lower 27.0 per cent). Therefore, the general business activity index was zero (0). However, as in the previous survey, the majority of the firms (46.0 per cent) believed that economic activity would remain the same relative to 2003. Firms in the services sector were more optimistic with the index showing (+9) than those in industry (-26).

The majority of panel firms expect inflation to be at a much lower level (45.0 per cent) against 33.0 per cent with higher inflationary expectations. In the previous survey, the majority of the respondents had higher inflationary expectations (70.0 per cent) compared to 6.0 per cent with lower expectations.

6.0 Real Sector

Given this year's good rains, which should boos agricultural production, coupled with the expected robust growth of building and construction, mining and quarrying, tourism and re-exports, on balance, growth in GDP was revised upwards to 7.1 per cent from 6.0 per cent in 2004.

Risks

The projected growth rate of 7.1 per cent could, however, be undermined by the following:

- Further increase in world oil prices which could negatively impact the terms of trade;
- Less-than-expected increase in tourist arrivals;
- Higher than projected budget deficit financed by the Central Bank and the concomitant increase in inflationary pressures.

7.0 Fiscal Developments

With a budgetary projection of D1202.6 million for the end-June 2004 quarter, total revenue and grants decreased by 4.2 per cent to D831.3 million from D867.7 million in the first quarter of 2004. Domestic revenue which comprised tax and non-tax revenue, increased to D671.5 million or 5.1 per cent from the previous quarter.

Total expenditure and net lending decreased to 897.4 million or 22.92 per cent and was within the projected ceiling of D1378.1 million The budget deficit (excluding grants and without HIPC) on commitment basis, narrowed considerably from D479.4 million (3.9 per cent of GDP) in the first quarter to D177.0 million (1.4 per cent of GDP) in the second quarter and was within the target to D244.3 million. Similarly, the fiscal deficit (including grants) on commitment basis, fell from D296.6 million (2.4 per cent of GDP) in the first quarter to D66.3 million (0.5 per cent of GDP) in the second quarter and was within the target D175.6 million.

The basic primary balance (domestic revenue minus total expenditure and net lending excluding interest payments and externally funded capital expenditure) as a percentage of GDP was 2.3 per cent in the second quarter relative to 2.2 per cent in the first quarter.

To finance the budget deficit, there was a net borrowing of D79.4 million and D129.8 million from foreign sources and the domestic banking system respectively. At the same time there was a net repayment of D74.6 million to the non-bank public.

8.0 Financial System Soundness Indicators

Capital Adequacy

The industry Risk-weighted Capital Adequacy Ratio dropped slightly from 27.22% in March 2004 to 26.14% in June 2004. This was due to decreased Capital and Reserves Offsetting the decline in total Assets.

Notwithstanding the decline in Capital Adequacy Ratio, the banking sector was comfortably above the required minimum of 8 per cent. The lowest ratio was 11.1 per cent and the highest 58.7 per cent in June 2004.

Asset Quality

Total Assets for the industry stood at D5894.27 million in June 2004 with loans and advances accounted for 24.9 per cent of the total.

Non-performing loans stood at D155.63 million at end-June 2004, or 10.6 per cent of gross loans and advances. This was lower than the 15.87 per cent recorded in the first quarter. The improvement was as a result of the transformation of some dud loans into performing facilities

Earnings and Profitability

The banking industry experienced a drastic decline in its profitability. Three of the banks reported losses after tax while the other three reported lower profit after tax. The highest reported profit was D31.3 million and the biggest reported loss was D2.1 million. The deterioration in earning was mainly due to half-yearly interest payments on deposits as well as increased operating expenses.

Liquidity

Average liquid Assets Ratio for the industry stood at 75.2 per cent in June compared with 73.9 per cent in March 2004. This ratio measures available liquid assets to meet demand for cash. The substantially high ratio is a clear indication that the banking sector is awashed with liquidity. The lowest liquidity ratio was 61.9 per cent whilst the highest ratio was 85.0 per cent.

9.0 Inflation Report

Consumer Price Index (CPI)

End-period inflation, as measured by the consumer price index of low-income population of Banjul and Kombo St. Mary area, declined from 21.1 per cent in August 2003 to 14.7 per cent at end-August 2004. Average inflation rate at end-August (12 month moving average) stood at 16.9 per cent.

The first measure of core inflation, which strips out fuel, light and transportation, showed inflation declining from 19.4 per cent in August to 12.5 per cent in August 2004.

The second measure of core inflation which excludes energy, transportation and volatile food items ("meat, poultry, eggs and fish" "tobacco and tobacco products", "cereals and cereal products", and processed foods") also shows a decline in inflation from 12.7 in August 2003 to 6.6 per cent in August 2004.

End-December 2004 inflation forecast is 12.3 per cent premised on stable exchange rate for the entire 2004, money supply growth of 20.0 per cent and government expenditure and net lending as a percentage of GDP of 25.5 per cent.

Factors that might affect the inflation dynamics in 2004

i Significant domestic demand pressure in 2004 due to expansionary fiscal policy;

ii Marked exchange rate movements. This would impact inflation directly i.e via imported inflation;

iii The budget financing requirements may increase, including Central Bank financing;

iv Sustained increase in world oil prices which may put pressure on the exchange rate and inevitably consumer prices;