MINUTES OF THE MONETARY POLICY COMMITTEE MEETING

August 05, 2015

The Third meeting of the Monetary Policy Committee (MPC) of the Central Bank of The Gambia (CBG) in 2015 took place in the Conference Room of the Bank on Wednesday August 5, 2015.

Present were:

Mr. Amadou Colley	Governor, (Chairman)
Mr. Basiru A.O Njai	First Deputy Governor, Member
Mrs. Oumie Savage-Samba	Second Deputy Governor, Member
Mr. Abdoulie Jallow	Permanent Secretary, MoFEA, Member
Mr. Paul Mendy	Director II, Financial Supervision Department (FSD), Member
Mr. Ismaila Jarju	Director, Economic Research Department (ERD), Member
Mr. Mbye Jammeh	Director, Banking Department (BD), Member
Mr. Alhagie Taal	Director, Macroeconomic Directorate, MOFEA, Member
Mr. Sulayman Ceesay	Senior Economist/Statistician, ERD, (Secretary)

In attendance were:

Mr. Ousainou Corr	Director, Finance Department
Mrs. Haddy Joof	Director, Admin Department
Mr. Omar Jaata	Foreign, Department
Mr. Pa Alieu Sillah	Director, Insurance Department
Mr. Bai Senghor	Director, Microfinance Department
Mrs. Maimuna John-Sowe	Deputy Director, ERD
Mr. Abdoulie Janneh	Economist, NCC
Mrs. Annetta Riley	Principal Banking Officer, BD
Mr. Lamin Jarjue	Principal Banking Officer, BD
Mr. Karafa Jobarteh	Principal Officer, Foreign Department
Mr. Sheriff Touray	Senior Economist, ERD
Mr. Sulayman Bruce	Senior Economist, ERD

Mr. Yaya Cham	Senior Economist, ERD
Mrs. Aji Adam Njie	Economist, ERD
Mr. Khalilu Bah	Economist, ERD
Ms. Ya-Maram Sosseh	Bank Examiner, FSD
Mr. Babucarr Jammeh	Bank Examiner, FSD

<u>Opening Remarks by Chairman</u>

After observing silent prayers, the Governor and Chairman of the MPC welcomed the Committee members and attendees to the 56th meeting of the MPC. He thanked the members of the MPC for their insightful contributions to the decision on the reserve requirement (RR) and net open position (NOP) limits. With no matters arising, the meeting proceeded with presentations and discussions on the world economic outlook, real sector developments, fiscal developments, balance of payments (BOP), exchange rate developments, money market developments, monetary developments, financial stability and the inflation outlook.

World Economic Outlook

Since the previous meeting of the Monetary Policy Committee (MPC), the global economic environment has been characterized by heightened uncertainty relating to the debt crisis in Greece, sharp decline in equity prices in China and slowdown in economic growth.

The International Monetary Fund (IMF) revised its forecast for global growth for 2015 down from what was predicted in April 2015 World Economic Outlook. Growth is projected at 3.3 percent in 2015, lower than the 3.4 percent in 2014. Growth in advanced economies is projected to grow from 1.8 percent in 2014 to 2.1 percent in 2015. In the United States (US), economic growth accelerated to 2.3 percent in the second quarter of 2015 owing primarily to the pickup in consumer spending which offset the drag from soft business spending on equipment. Also, first quarter gross domestic product (GDP), previously reported to have contracted by 0.2 percent, was revised upwards to a growth rate of 0.6 percent.

The steady but slow improvement in the Euro area continued, following better-than-expected output in the first quarter. The IMF predicts the Euro area to grow by 1.5 percent, unchanged from the April forecast. However, the outlook for the region would depend in part on avoiding negative spillovers from the Greece debt crisis.

Growth in Japan is expected to remain positive, but subdued. The economy expanded by 1.0 percent in the first quarter of 2015, after an economic contraction in the fourth quarter of 2014. Growth for the entire 2015 is projected at 1.7 percent compared to a contraction of 0.1 percent in 2014.

Growth in the UK economy is projected at 2.4 percent in 2015 and 2.2 percent in 2016. The economy grew faster than previously thought in the first half of the year after it emerged that the construction sector performed better than previously estimated.

The Chinese economy grew by 7.0 percent year-on-year to the second quarter, but some moderation is expected in the coming quarters. The Chinese stock market plunged with the Shanghai Composite Index declining by 30.0 percent from its peak. Although the impact on the broader economy is expected to be relatively limited, it does point to some fragility in the financial sector. The IMF forecast the Chinese economy to grow by 6.3 percent in 2016 and 6.0 percent in 2017.

Sub-Saharan Africa is expected to grow by 4.2 percent in 2015 down from 4.6 percent in 2014. In the previous years, the main growth drivers were strong mining and infrastructure investment, private consumption and robust external sector mainly driven by commodity exports to China. The slow down in China and the concomitant decline in commodity prices, including oil since mid-2014 dented output.

Global inflation remains benign. Prices, particularly in the advanced economies, remain close to zero reflecting in the main declining commodity prices, including oil. As a result, monetary policy stances in most advanced and emerging market economies have either remained unchanged or have become more accommodative.

Commodity prices continue to decrease with the FAO Food Price Index averaging 165.1points in June 2015, down 1.5 points (0.9 percent) from the previous month and about 44.0 points (21.0 percent) from June 2014.

International oil prices also weakened following higher output by Saudi Arabia, the prospects of resumption of oil exports by Iran and the slowdown in global output. Prices decreased to about US$50 per barrel in the first week of August 2015.

The Committee noted the advice of the IMF that the Federal Reserve should delay the anticipated increase of the Federal Funds Rate. The Committee agreed that the IMF is spot on in that for the sake of international cooperation and given the slowdown in global growth in particular, increasing the policy rate would be a drag on global economic activity. More specifically, increasing interest rates in the US may lead to capital outflows from emerging markets to the US thus putting pressure on their external sectors and currencies. However, some Committee members indicated that the Federal Reserve has the responsibility to take policy actions to support the US economy despite the impact such measures may have on the global economy.

The Committee commented that what is happening in Greece is a cautionary reminder that debt to GDP that is exceedingly high tends to sap the vitality of the economy. In other words, there is nothing more anti growth than debt that is unsustainable. However, the Committee also noted that even though Japan's debt to GDP of 246.0 percent is higher than Greece's debt to GDP of 173.0 percent, Japan's 10-year bond attracts a yield of only 0.4 percent compared to Greece's yield of 11.0 percent. This was attributed to the fact that investors have greater confidence that Japan can manage its debt which may not be true of Greece.

The Committee welcomed the growth outlook in the UK and Euro area, the principal sources of tourists cognizant of the income elasticity for travel expenditure estimated to be as high as 2 to 3. That is, if incomes increased by 1.0 percent in real terms, expenditure on foreign travel increases by 2.0 to 3.0 percent and vice versa.

Real Sector Developments

The Gambia Bureau of Statistics (GBoS) revised downwards its growth estimate of the Gambian economy from 1.6 percent to 0.5 percent in 2014 attributed to the higher-than-expected contraction in agricultural production by 8.4 percent. Economic output is projected to expand by 7.5 percent in 2015 premised on the expected rebound in tourism and agriculture.

The Committee indicated that based on recent information on hotel bookings, expectations are that the tourism sector would rebound markedly. Agricultural output is also expected to increase, albeit subject to plentiful and well distributed rainfall. Some Committee members expressed the view that although agriculture has the potential to strongly support economic growth, it is inefficient and unproductive. Raising output requires massive investment in quality inputs, infrastructure, extension services and more importantly building agricultural resilience in the face of climate change and weather shocks.

Fiscal Developments

Preliminary data on government fiscal operations indicate that in the first half of 2015, total revenue and grants amounted to D5.23 billion, slightly lower than the projection of D5.43 billion. Domestic revenue, comprising tax and non-tax revenue totaled D3.83 billion, an increase of 17.0 percent from the outturn in the first half of 2014. Tax revenue rose to D3.46 billion, or 27.2 percent reflecting the increase in both direct and indirect taxes by 10.0 percent and 35.0 percent to D924.1 million and D2.53 billion respectively. Non-tax revenue and grants also increased to D550.70 million and D1.46 billion, or 48.4 percent and 36.4 percent from the corresponding period of 2014.

Total expenditure and net lending amounted to D6.06 billion, significantly higher than the projected D5.61 billion. Current expenditure increased to D3.91 billion, or 17.1 percent from the outcome in the first half of 2014 attributed mainly to the 80.7 percent increase in interest payments. External and domestic interest payments rose by 158.0 percent and 70.0 percent respectively. Capital expenditure also increased to D2.15 billion, higher than the projection of D1.73 billion and the D1.72 billion outturn in the first half of 2014. Capital expenditure was principally externally financed (89.9 percent) and the remainder was funded by Gambia Local Fund (GLF).

The overall budget balance on cash basis (including grants) was a deficit of D829.8 million (5.0 percent of GDP) compared to the deficit of D729.8 million (4.0 percent of GDP) in the first half of 2014.The deficit was financed by both external and domestic sources.

The Committee underscored that although revenue performed quite well expanding by 17.0 percent, expenditure and net lending grew at a stronger pace of 20.0 percent. The Committee reiterated the need for fiscal consolidation ideally tilted towards spending cuts. This is because spending cuts tend to do less damage to the economy than tax rises.

The Committee was informed that one of the reasons for the higher-than-projected expenditure is that some of the reforms such as reducing / downsizing the number of embassies, and vehicle policy etc were yet to kick in.

The Committee emphasized that shocks cannot be predicted with certainty and therefore it is absolutely critical to build resilience. Strong fiscal fundamentals provide the fiscal space to cope with domestic and external shocks.

External Sector Developments

Balance of payments (BOP) estimates for the first half of 2015 indicate an overall deficit of US$30.5 million, higher than the deficit of US$19.0 million in corresponding period of 2014.

The current account deficit widened to US$ 65.7 million from the deficit of US$11.0 million in the first half of 2014. Of the components of the current account, the merchandise trade deficit widened to US$114.6 million compared to the deficit US$104.5 million in the first half of 2014. Imports rose to US$ 179.0 million or 3.2 percent whilst exports contracted to US$54.1 million, or 0.6 percent.

The services account surplus decreased to US$36.5 million from the surplus of US$59.3 million in the corresponding period in 2014 reflecting in the main decreased income from tourism. Income from tourism declined to US$53.5 million during the review period compared to US$71.0 million recorded in the corresponding period in 2014.

The income account deficit is estimated to have widened to US$14.6 million relative to the deficit of US$10.7 million in the corresponding period in 2014, owing to higher interest payments. Current transfers are estimated at a surplus of US$27.2 million, lower than the surplus of US$44.9 million in the first half of 2014. Although transfers to general government increased by 6.21 percent, workers' remittances decreased slightly by 1.3 percent to US$35.4 million.

The capital and financial account is estimated at a surplus of US$29.4 million, down from the surplus of US$63.2 million in the first half of 2014. The capital account surplus increased to US$37.8 million, or 9.8 percent. The financial account, in contrast, decreased from US$28.8 million in the first half of 2014 to US$8.4 million during the period under review.

The Committee underscored that the unfavorable external sector, coupled with the expansionary stance of fiscal policy exerted huge pressures on the foreign reserve of the CBG. As at end June 2015, net international reserve (NIR) stood at US$46.92 million against the target of US$77.7 million.

The Committee expressed worry that the current account deficit is largely financed by draw down of the reserves as opposed to the recent past when the deficit was financed by non-debt flows, particularly foreign direct investment (FDI). The Committee underscored the importance of creating the right environment to attract FDI, including a predictable policy regime, macroeconomic stability, solid property rights and good infrastructure.

Exchange Rate Developments

Year-on-year to end-June 2015, volume of transaction in the foreign exchange market, measured by aggregate purchases and sales, increased to US$1.28 billion compared to US$1.25 billion a year ago.

In May 2015, the Government of The Gambia issued an exchange rate directive, which limited the flexibility of the exchange rate. Consequently, the Dalasi appreciated against all the major currencies. In the year to end-June 2015, the Dalasi strengthened against the US Dollar by 5.6 percent, Euro (24.4 percent) and Pound Sterling (8.1 percent).

Some Committee members noted that senders of remittances are rate sensitive and to the extent that the Dalasi has suddenly appreciated, remittance flows through formal channels is likely to decrease. Some members argued that because the flows are mostly passing through informal channels they are not captured by the Central Bank of the Gambia (CBG).

Some Committee members indicated that the appreciation of the Dalasi may negatively impact the tourism sector. If hotels become expensive because the domestic exchange rate is not maintained at a competitive level, the firms putting together package tours may simply switch to another country. Put differently, the high price of the Dalasi, which is meant by a strong Dalasi, is not desirable in the face of the BOP shocks.

Money Market Developments

As at end-June 2015, the domestic debt stood at D19.2 billion, or 30.4 percent from a year ago. This was mainly the result of the 9.9 percent increase in outstanding Treasuring bills and the issuance of 20-year bond held by the CBG

According to the distribution of Treasury bills by holder, deposit money banks held 69.4 percent of the debt, the non-bank (23.3 percent) and CBG (7.3 percent).

Yields on all Government short-dated securities increased. The yields of 91-day, 182-day and 364-day Treasury bills rose from 14.31 percent, 15.95 percent and 18.12 percent in June 2014 to 17.19 percent, 18.46 percent and 21.45 percent respectively in June 2015. Also, the yields on the 91-day, 182-day and 364-day Sukuk-Al-Salam (SAS) rose to 17.58 percent, 18.44 percent and 20.54 percent in June 2015 compared to 14.86 percent, 16.4 percent and 18.34 percent in June 2014.

The Committee noted that success in selling debt depends on the confidence the buyers have on the issuer and the risk that there would not be a default. And to the extent investors have confidence on the capacity of the Government of the Gambia to borrow and repay, the demand for Treasury bills and SAS remain solid.

The Committee reiterated the need to first stabilize and then reduce the large domestic debt considering that it is not only a drag on growth but has paralyzed fiscal policy. In essence, the time has come to re-order fiscal priorities and to implement structural reforms to increase growth, the best means of addressing the debt problem.

Monetary Developments

The pace of monetary expansion accelerated in the year to end-June 2015. Money supply grew by 11.6 percent year-on-year to end-June 2015 compared to 8.1 percent a year ago. This was mainly as a result of the robust growth in the net domestic assets (NDA) of the banking system by 30.4 percent from 12.6 percent a year earlier. The main driver of the growth in the NDA was net claims on government by the banking sector, which rose by 39.3 percent from 25.3 percent a year ago. Claims on public entities and the private sector both contracted by 29.6 percent and 19.7 percent respectively. The net foreign assets of the banking system, on the other hand , contracted by 40.1 percent relative to the slight contraction of 2.5 percent a year ago.

Of the components of money supply, narrow money, comprising currency outside banks and demand deposits, rose to D10.9 billion, or 14.7 percent. Both currency outside banks and demand deposits rose by 10.3 percent and 17.1 percent respectively.

Quasi money, comprising savings and time deposits, grew at a slower pace of 8.4 percent, but higher than the 2.4 percent a year ago. Both savings and time deposits grew by 9.8 percent and 5.3 percent respectively.

Growth in reserve money, the Bank's operating target, decelerated to 11.9 percent, significantly lower than the 19.7 percent in June 2014. This was mainly as a result of the 84.0 percent contraction in the NFA of the CBG. In contrast, the NDA of the CBG increased at a strong pace of 134.7 percent on top of the 97.2 percent growth in June 2014.

The Committee noted that despite pressures on the Dalasi, the Gambian economy is not dollarized as is the case of some African countries. For instance, the ratio of foreign currency deposit to money supply was only 19.7 percent in June 2015 indicating that large amounts of US Dollar are not held by the public.

The Committee agreed that growth in reserve money and money supply would have been significantly higher, but for the offsetting contraction in the NFA of the

CBG and the banking system respectively. Notwithstanding, money supply growth exceeded money demand with the attendant implication on general prices.

Developments in the Banking Sector

The banking sector continues to be stable and sound. Capital and reserves totaled D3.95 billion in the second quarter of 2015, slightly lower than the D3.96 billion in the first quarter. However, capital adequacy ratio averaged 38.0 percent in the second quarter compared to 33.0 percent in the first quarter and higher than the minimum requirement of 10.0 percent.

Deposit liabilities increased to D16.95 billion or 1.0 percent from the first quarter attributed primarily to the 6.0 percent increase in demand deposits, Savings and time deposits, on the other hand, contracted by 2.0 percent and 1.0 percent respectively. Although the liquidity ratio decreased to 86.0 percent in the second quarter compared to 90.0 percent in the first quarter, it was over and above the liquidity requirement of 30.0 percent.

The assets of the industry rose to D29.04 billion, or 4.0 percent from the previous quarter. Loans and advances, accounting for 20.0 percent of total assets, decreased to D5.81 billion, or 5.0 percent owing in part to decreased lending to the private sector. Private sector credit, representing 77.0 percent of loans and advances, declined to D4.46 billion, or 4.0 percent. Despite the contraction in credit, the non-performing loans (NPLs) ratio, increased to 11.0 percent compared to 6.0 percent in the first quarter.

The industry recorded a net profit of D0.15 billion in the second quarter, a decrease of 2.0 percent from the previous quarter. The return on assets (ROA) and return on equity (ROE) declined to 2.3 percent and 15.4 percent compared to 2.5 percent and 15.9 percent in the last quarter.

The Committee broadly agreed that overall the banking system is safe and sound evidenced by the high capital adequacy ratio, ample liquidity and the profitability of the industry. Some of the banks have very high ROE, an indication that they are very profitable.

Some Committee members noted the decrease in private sector credit and commented that it was a result of a combination of factors, including high interest rates, crowding out effect of government's borrowing and the challenges confronting the Gambian economy such as the slowdown in economic activity.

Inflation Outlook

Consumer price inflation, measured by the National Consumer Price Index, accelerated to 7.2 percent in June 2015 compared to 5.4 percent a year ago. The main driver of headline inflation was consumer food prices which rose from 6.2 percent in June 2014 to 9.1 percent in June 2015. Meat and bread and cereals rose by 6.4 percent and 22.7 percent respectively. Non-food inflation, on other hand, decreased marginally to 4.3 percent compared to 4.4 percent in June 2014. Core inflation, which excludes prices of energy and volatile food items, accelerated strongly to 7.6 percent from 5.5 percent in June 2014.

The Committee noted that much of the inflation is due to temporary factors such as the weak Dalasi, increase in prices of volatile food items because of the delayed rainfall in 2014, etc. Thus, monetary policy should target core inflation. However, to the extent that the acceleration in core inflation mirrors that of headline inflation, it may not matter which of the prices is targeted.

The Committee agreed that the exchange rate is an important determinant of inflationary pressures and owing to the challenges to increase the supply of foreign exchange in the short term, policy should be directed at reducing demand. However, reducing import demand for instance is complicated by the fact that it is inelastic and besides even though the CBG can tighten monetary policy it is not in charge of fiscal policy.

Decision

The MPC is concerned that consumer price inflation continued to exceed the target of 5.0 percent and inflation is forecast to remain at elevated levels. Failure to act against these heightened pressures may cause prices to accelerate further and the high inflation expectation to become more entrenched.

Against this backdrop, the MPC has decided to continue the tight monetary policy stance by: (I) Keeping the policy rate unchanged at 23.0 percent; and (II) maintain the reserve requirement ratio at 15.0 percent of deposit liabilities, but to eliminate the cash-in-vault of commercial banks as a reserve asset for the calculation of cash reserve requirement (CRR) with effect from September 01, 2015. The MPC would continue to monitor domestic and international developments and take action as appropriate.