MINUTES OF THE MONETARY POLICY COMMITTEE MEETING

AUGUST 31, 2010

The third meeting of the Monetary Policy Committee (MPC) of the Central Bank of The Gambia (CBG) in 2010 took place in the Conference Room of the Bank.

Present were:

Mr. Momodou B. Saho	Governor, Chairman, Member
Mr. Basiru A.O Njai	First Deputy Governor, Member
Mrs Oumie Savage Samba	Second Deputy Governor, Member
Mr. Amadou Colley	Director, Banking Department, (BD) Member
Mr. Essa Drammeh	Deputy Director, (FSD) Member
Mr. Ismaila Jarju	OIC, Research Department, (ERD) Member
Mr. Abdoulie Jallow	Deputy Permanent Secretary, Ministry of Finance
Mr. Momodou Sabally	Director of Budget, Ministry of Finance
Mr. Bakary Jammeh	Principal Economist, ERD (Secretary)

In Attendance were:

Mr. Omar Jaata	Director Foreign Department
Mr. Ousainou Corr	Director, Finance Department
Mr. Bai Senghor	Director, Micro-Finance Department
Mr. Pa Alieu Sillah	Commissioner for Insurance
Mr. Mbye Jammeh	Deputy Director, Banking Department
Mr. Paul Mendy	Deputy Director, FSD
Mr. Abdoulie Jallow	Deputy Director, FSD
Mr. Ebrima Wadda	Principal Economist, ERD
Mrs Ida Fye-Touray	Principal Banking Officer, FSD
Mrs. Maimuna John-Sowe	Principal Economist, ERD
Mr. Karamo Jawara	Principal Banking Officer, BD
Mr. Momodou Lamin Jarjue	Senior Banking Officer, BD
Mr. Karafa Jobarteh	Senior Officer, Foreign Department

Mr. Sheriff Touray	Economist, ERD
Mr. Sait Mboob	Economist, ERD
Mr. Paul Bruce	Economist/Econometrician/ ERD
Mr. Yaya Cham	Economist, ERD
Mr. Sulayman Ceesay	Economist/Statistician, ERD
Ms. Binta Beyai	Economist, ERD
Mr. Abdoulie Touray	Banking Officer, FSD

The Monetary Policy Committee (MPC) meeting was held at the Bank's Conference Room on Wednesday, August 31, 2010. In his opening remarks, the Governor and Chairman of the MPC welcomed all those present at the meeting. Thereafter, the Committee reviewed, amended and adopted the minutes of the previous meeting. This was followed by presentations and discussions on international economic developments, balance of payments, foreign exchange, monetary and money market developments as well as Government fiscal operations, inflation, financial stability report and private sector business sentiment survey.

1.0 International Developments

The IMF projects world economic output to increase by 4.5 percent in 2010 and 4.25 percent in 2011. Driven by robust growth in Asia and stronger-than-expected private demand in some of the major industrial countries, the global economy expanded by 5.0 percent in the first three months of 2010.

The US economic recovery is projected to proceed more slowly than in previous cycles, reflecting somewhat weaker growth in the rest of the world, the unwinding of fiscal stimulus measures and the on-going deleveraging by households and financial institutions. In the second quarter of 2010, the US economy grew at an annualized rate of 2.4 percent compared to the 3.7 percent in the previous quarter. The IMF projects that the US will grow by 3.3 percent in 2010 and 2.9 percent in 2011.

Economic growth in the Euro area is projected at 1.0 percent in 2010 and 1.3 percent in 2011. Germany and France, the two biggest economies in the Euro area, posted higher-than-expected growth rates. The French economy grew by 0.6 percent and Germany's by 2.2 percent in the second quarter of 2010, the fastest quarterly growth in more than 20 years. The strong growth was supported by exports which benefitted from a weaker Euro.

The UK economy is forecast to grow by 1.2 percent in 2010 and 2.1 percent in 2011. Government plans to cut public spending have hit confidence. This, coupled with low levels of bank lending has constrained economic growth.

Economic growth in Asia has been revised upwards to 7.5 percent in 2010. The Chinese economy is forecast to grow by 10.5 percent in 2010, before slowing to about 9.5 percent in 2011 thanks to strong rebound in exports and rising domestic demand.

Africa's economy grew by only 2.5 percent in 2009 after averaging 6.0 percent between 2006 and 2008. Growth is projected to expand by 4.5 percent in 2010 and 5.2 percent in 2011 reflecting on-going rebound in global trade, rising mineral prices, prudent management of public finances and implementation of structural reforms that improve the business and investment climate.

Prices of many commodities fell during the financial market shocks in May and June 2010 reflecting in part expectations of weakening global demand.

The IMF projects oil prices to average US$75.0 a barrel in 2010 and US$77.5 in 2011, lower than the initial projection of US$83 in April 2010. Non-fuel commodity price index has remained broadly unchanged partly reflecting stronger-than-expected market conditions through April 2010.

Inflationary pressures are expected to remain broadly subdued in advanced economies reflecting lower levels of capacity utilization and well anchored inflationary expectations. In emerging and developing economies, inflation is expected to accelerate to 6.25 percent in 2010 before decelerating to 5.0 percent in 2011.

The Committee commented that the best characterization of the global economy is that though showing signs of recovery, it is not yet self sustaining. Households, banks and governments in a number of advanced economies are repairing their balance sheets. As a result, domestic demand is not as robust compared to past cycles. For example, it is estimated that the US personal savings rate has recently increased from an average of 1.8 percent over 2005 – 2007 to about 3.5 percent in 2009. It is expected to reach 5.0 percent in 2011.

The Committee indicated that sustained recovery in Africa is predicated on sustaining the macroeconomic stability, continued implementation of structural reforms and robust global recovery.

The Committee noted the increase in non-oil commodity prices and agreed that it has impacted prices in The Gambia. The committee advised on the need to implement prudent policies going forward in order not to put additional pressure on prices.

The Committee agreed that slower-than-expected growth in Europe should negatively impact Gambian tourism. In fact, data indicate that tourist arrivals actually declined in the first 9 months of 2010 compared to the same period in 2009.

2.0 Balance of Payments (BOP)

Preliminary BOP estimates indicate an overall surplus of US$48.4 million in the first quarter of 2010 compared to a deficit of US$32.8 million during the same period in 2009.

The goods account deficit narrowed to US$13.5 million in quarter 1, 2010 from US$26.1 million in quarter 1, 2009, Exports grew by 23.0 percent while imports contracted by 8.8 percent.

The services account surplus increased to US$15.5 million from US$14.0 million in the corresponding quarter of 2009, reflecting in part increased income from communication services which rose from US$2.0 million in quarter 1, 2009 to US$3.48 million in quarter 1, 2010. Travel income totaled US$17.4 million in quarter 1, 2010, lower than the US$23.4 million in quarter 1, 2009.

The income account balance recorded a small surplus of US$0.34 million in quarter 1, 2010 compared to a deficit of US$2.86 million in quarter 1, 2009. However, the transfer account surplus surged from US$10.85 million in quarter 1, 2009 to US$45.81 million in quarter 1, 2010.

The capital and financial account balance was a surplus of US$0.18 million in quarter 1, 2010 from a deficit of US$28.7 million in quarter 1, 2009.

The Committee noted that the overall BOP surplus in quarter 1, 2010 may explain the stability of the Dalasi during the first quarter. However, the overall BOP surplus realized in quarter 1, 2010 is likely to be reversed in quarter 2, 2010 which may explain the weakening of the Dalasi in quarter 2, 2010.

It was commented that to the extent that exports grew at a faster rate than imports should impact positively on growth in 2010.

3.0 Foreign Exchange Developments

Volume of transaction in the foreign exchange market increased to D25.2 billion in the year to end-July 2010 from D20.2 billion a year earlier. Commercial banks accounted for over 94.0 percent of market turnover.

According to the nominal effective exchange index, the Dalasi depreciated against the basket of currencies by 6.0 percent in July 2010 from end-December 2009. Against individual currencies, the Dalasi depreciated against the pound sterling by 5.8 percent and 9.3 percent against the Dollar, but appreciated against the euro by 5.2 percent.

The Committee noted that the exchange rate of the Dalasi largely reflect macroeconomic fundamentals. In quarter 1, 2010 economic fundamentals were quite strong, but there was deterioration in quarter 2, 2010. For example, both monetary and fiscal policies were expansionary evidenced by the strong growth in some of the monetary aggregates and the marked increase in the budget deficit of about 1.6 percent of GDP (including grants) in the second quarter of 2010.

The Committee commented that though the exchange rate of the Dalasi is market-determined, it cannot be treated with benign neglect. If circumstances warrant, the CBG, which is responsible for exchange rate policy, is obliged to take action to stabilise the exchange rate.

4.0 Fiscal Developments

The Government's fiscal position weakened in the first half of 2010. The budget deficit (including grants) widened to 5.2 percent of GDP compared to 2.9 percent of GDP in the corresponding period in 2009.

Revenue and grants totaled D2.5 billion, slightly higher than the D2.35 billion in the first half of 2009. Revenue amounted to D2.11 billion (19.2 percent of GDP), representing an increase of 1.98 percent from the first half of 2009. Tax revenue, which totaled D1.8 billion, or 87.3 percent of total revenue, declined marginally by 0.6 percent. Direct taxes increased to D601.0 million, or 10.5 percent while indirect taxes decreased by 5.2 percent to D1.23 billion. Taxes on international trade and duty in particular declined by 9.4 percent and 25.1 percent respectively.

Non-tax revenue and grants increased to D268.0 million and D298.6 million, or 23.9 percent and 4.1 percent respectively.

Total expenditure and net lending is estimated to have increased to D2.98 billion, or 11.2 percent from the first half of 2009. Both current and capital expenditure increased by 6.0 percent and 37.6 percent respectively.

The Committee welcomed the fact that there has been a reorientation of expenditure with a bias towards capital expenditure. However, the Committee expressed concern over the higher-than-projected budget deficit of 6.0 percent of GDP in the first half of 2010 and the manner it was financed. The deficit was largely monetized which could lead to the build up of inflationary pressures.

The Committee observed that although expenditure was contained and was largely within budget, the revenue outcome was disappointing. It was indicated that looking forward, it is expected that the budget deficit would narrow predicated on a projected increase in revenue in the fourth quarter of 2010 and the administrative measures put in place to reduce expenditure.

5.0 Money market Developments

As at end-July 2010, the domestic debt increased to D7.7 billion, or 8.0 percent from July 2009. The increase in the debt stock was mainly as a result of the 26.6 percent increase in Government's overdrawn position with the CBG. Outstanding Treasury bills and Sukuk-Al-Salaam combined, accounting for 68.4 percent of the debt, increased by 5.4 percent to D5.2 billion.

According to the data on the distribution of Treasury Bills and SAS by maturity, one-year bills accounts for 64.6 percent of the outstanding stock, 182-day bills (18.1 percent) and 91-day bills (17.3 percent).

The yield on all the profiles declined. The average yield on the 91-day bill, 182-day bill and 364-day bills decreased from 10.16 percent, 11.22 percent and 13.31 percent in July 2009 to 9.41 percent, 10.33 percent and 13.1 percent in July 2010 respectively.

The Committee noted that the net issuance of Treasury bills and SAS was only D9.4 million between January to July 2010. This mainly reflected the decision of the MPC, taking a cue from the Memorandum of Economic and Financial Policies (MEFP), to reduce the stock of domestic debt with a view to reducing interest rates. This was, however, largely offset by the 26.6 percent increase in the Treasury Main Account overdraft.

The Committee commented that the yield on the maturities would have been higher, but for the recourse by Government to ways and means i.e. borrowing from the CBG and paying no interest.

6.0 Real Sector

The Gambian economy is forecast to grow by 5.0 percent in 2010, but lower than the 5.6 percent in 2009. As a share of GDP at factor cost, agriculture is projected to account for 26.2 percent of GDP, industry (13.0 percent) and services (60.7 percent).

The Committee noted that economic activity is likely to be subdued in 2010 relative to 2009, but it is encouraging that it would exceed the Sub-Saharan projected average of 4.1 percent.

7.0 Monetary Developments

In the year to end-July 2010, money supply grew by 20.6 percent compared to 18.4 percent a year earlier. Both the net foreign assets (NFA) and the net domestic assets (NDA) of the banking system increased by 6.0 percent and 27.1 percent respectively. Of the components of broad money, narrow money increased by 12.6 percent and quasi money by 27.7 percent.

The breakdown of NDA of the banking system indicated that domestic credit grew by a robust 27.1 percent, higher than the 23.1 percent a year earlier. Claims on government, net, and credit to the private sector rose by 28.1 percent and 29.4 percent respectively.

Reserve money increased by 20.0 percent compared to 1.8 percent in July 2009. Both the NDA and the NFA of the CBG increased by 410.3 percent and 8.2 percent respectively.

The Committee expressed concern of the high growth of the monetary aggregates and their likely impact on prices and advised on the need for fiscal rectitude. Some Committee members were of the view that given the build-up in inflationary pressures, the stance of policy should be contractionary to counteract the expansionary fiscal policy.

The Committee commented that it appears the monetary approach to BOP is at work. The increase in money supply over demand caused a decrease in real interest rates. As a result, credit expanded, increased demand for goods and services, including import demand and ultimately a run-down of reserves.

8.0 Financial Stability Report

The banking sector remains concentrated with the three largest banks accounting for 58.9 percent, 62.8 percent and 51.9 percent of total assets, deposit liabilities and capital and reserves respectively in June 2010.

The Industry's total assets increased to D15.4 billion, or 17.3 percent from June 2009. Loans and advances, accounting for 29.2 percent of total assets, increased to D4.5 billion, or 22.7 percent.

Deposit liabilities increased to D13.8 billion, or 23.0 percent from June 2009. All categories of deposits increased with the exception of demand deposits.

Capital and reserves rose to D1.6 billion, or 7.7 percent. However, a number of banks failed to observe the minimum capital requirement. The average capital adequacy declined to 15.6 percent, lower than the 19.5 percent in June 2009.

The non-performing loans ratio was 16.7 percent in June 2010, higher than the 12.0 percent in June 2009. It is, however, noteworthy that the restructured loans accounted for about 42.5 percent of the NPLs.

The industry's earnings totaled D67.2 million in the second quarter of 2010 compared to D52.3 million in the corresponding quarter of 2009.

The Committee noted that though some of the soundness indicators have deteriorated, overall, the banking system remains fundamentally sound. In particular, though the average capital adequacy and the liquidity ratios have decreased, they exceeded the minimum prudential requirements.

The Committee expressed concern over the increase in non-performing loans attributed in part to high lending rates. The Committee noted that the reasons for high interest rates are mainly structural including the high cost of banking, high reserve requirement and the difficulty in realizing collateral.

9.0 Business Sentiment Survey

The majority of respondents (47.0 percent) indicated that economic activity was higher in quarter 2, 2010 compared to 30.0 percent that indicated that activity was lower. This implies a diffusion index of 13 percent.

At the company level, about 37 percent of respondents reported that activity in the second quarter of 2010 was higher compared to 33 percent that reported lower activity with a diffusion index of 4 percent.

The majority of respondents reported that sales, employment and profits were higher, but capital expenditure was lower.

About 57 percent of the respondents reported that current prices were higher compared to zero that indicated lower prices. Also, the majority of firms expect inflation to be higher in quarter 3, 2010.

The Committee noted the better-than-expected positive sentiment with respect to economic and business activity. This was attributed largely to favourable responses from industry firms. Service firms were largely pessimistic of overall economic and business activity.

10.0 Inflation

Headline inflation, measured by the National Consumer Price Index, was 6.2 percent in July 2010, higher than the 4.0 percent in July 2009.

Consumer food price inflation accelerated to 8.3 percent in July 2010, compared to 4.3 percent in July 2009. Non-food consumer price inflation was 2.9 percent in July 2010, lower than the 3.8 percent in July 2009.

Core inflation, which excludes prices of energy, utilities and volatile food items rose to 5.2 percent in July 2010 relative to the 4.6 percent in July 2009.

The Committee noted that inflationary pressures are accelerating and there is the likelihood that looking forward, the economy would be buffeted by significant price pressures. The confluence of monetisation of the budget deficit by the CBG, depreciation of the Dalasi and rising commodity prices are putting pressure on prices. The prognosis for inflation decreasing to low single digit in the fourth quarter is not good. In fact, it is likely that the end-December 2010 headline inflation target of 5.0 percent would not be realized.