MINUTES OF THE MONETARY POLICY COMMITTEE MEETING

AUGUST 27, 2009

The twenty-eighth meeting of the Monetary Policy Committee (MPC) of the Central Bank of The Gambia (CBG) took place in the Conference Room of the Bank on August 27, 2009

Present were:

Momodou B. Saho	Governor, Chairman, Member
Basiru A.O Njai	Deputy Governor 1, Member
Oumie Savage Samba	Deputy Governor 2, Member
Mr. Ousman Sowe	Financial Supervision Department, Member
Mr. Amadou Colley	Banking Services Department, Member
Mr. Ismaila Jarju	Economic Research Department, Member
Dr. Tamsir Cham	Ministry of Finance, Member
Mr. Serign Cham	PS II Ministry of Finance, Member
Mr. Momodou Sabally	Principal Economist, ERD, Secretary

In Attendance were:

Mr. Momodou Ceesay	Adviser to Governor
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
Mr. Bakary Jammeh	Principal Economist, ERD
Mrs. Anneta Riley	Senior Banking Officer, BD

Mr. Karafa Jobarteh	Senior Officer, Foreign Department
Mr. Abdou Ceesay	Senior Officer, Foreign Department
Mr. Mustapha Samateh	Bank Examiner, FSD
Mr. Amadou Barry	Bank Examiner, FSD
Mrs. Isatou Mendy	Economist, ERD
Mr. Saikouba Sisay	Economist, ERD
Mr. Sheriff Touray	Economist, ERD
Mr. Sait Mboob	Economist, ERD
Mr. Paul Bruce	Economist, ERD
Mr. Yaya Cham	Economist, ERD

The MPC reviewed 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, money market and financial stability developments as well as government fiscal operations and inflation.

(1) Developments in the International Economy

According to the latest World Economic Outlook, growth is projected to contract by 1.4 percent in 2009, before expanding by 2.5 percent in 2010. GDP in the advanced economies is expected to decline by 3.8 percent in 2009 and to grow by 0.6 percent in 2010.

The pace of contraction in the US economy is moderating. US GDP contracted at an annualized rate of 1.0 percent in the second quarter of 2009, compared to 6.4 percent in the first quarter. The monthly Inflation rate, measured by the Consumer Price Index, was 0.7 percent in June 2009, compared to -0.1 percent in March 2009. The Federal Reserve indicated that interest rates are likely to remain in the range of 0 to 0.25 percent for an extended period of time.

GDP in the Euro-area contracted by an annualised rate of 4.7 percent in the second quarter of 2009, compared to 1.5 percent in the corresponding quarter in 2008. The end period inflation rate was -0.7 percent in July 2009, compared to -0.1 in the preceding month. The European Central Bank (ECB) voted to keep the policy interest rate unchanged at 1.0 percent during its last meeting.

GDP in UK declined by 0.8 percent in the second quarter, lower than the contraction of 2.4 percent in the first quarter of 2009. Inflation decelerated to 1.8 percent in June 2009, down from 2.2 percent in the previous month. The Bank of England voted in July to maintain the policy rate at 0.5 percent and to review the quantitative easing policy.

Japan's economy grew by 0.9 percent in the second quarter of 2009, and at by an annualized 3.7 percent. This in effect meant that Japan is no longer technically in recession. Japan's inflation rate was -1.8 percent in June 2009 thanks to rising unemployment and falling incomes.

GDP in emerging and developing countries is projected to decline by 0.1 percent in 2009 before expanding by 0.7 percent in 2010.

China's economy grew at an annualized rate of 7.9 percent in June, up from 6.1 percent in the first quarter, helped by the government's stimulus package totaling $585 billion and the easing of the global economic contraction.

Growth in sub-Saharan Africa is projected to slow to 1.5 percent in 2009 from 5.5 percent in 2008, reflecting the slow down in global economic activity and the concomitant decrease in foreign inflows.

Reflecting primarily the slowdown in economic activity, inflationary pressures continue to ease. Global inflation decelerated to 1.7 percent in May 2009 from 6 percent a year earlier.

In advanced economies, headline inflation was negative in May 2009. In emerging and developing economies, headline inflation averaged 4.5 percent in May 2009, lower than 9.1 percent in May 2008.

As prospects for the global economy continue to improve, oil prices surged to more than $75 a barrel in August 2009. Sugar prices rose to 20.85 cents a pound in the first week of August 2009, the highest since April 1981 owing to crop failures in India and Brazil which reduced supply.

The Committee commented that available information indicates signs of global economic recovery. However, on the flip side, oil and food prices increased noticeably and if this trend continues there is bound to be increased inflationary pressure.

The Committee observed that the essence of counter cyclical polices is to increase demand, particularly public sector demand given that private consumption, the main driver of economic growth in advanced countries, has not only declined, but may take time to recover.

The Committee noted the slowdown in economic activity in the UK and agreed that it will be a damper on the Gambian economy given the large number of tourists from the UK. Tourism arrivals declined by about 25 percent in the year to end-April 2009 and the prospects for a strong recovery hinge on a return to growth in the main source countries.

The Committee recommended that in the future it would be useful to enrich the presentation on international developments by including competitiveness and terms of trade issues. Some Committee members believed that given the trend depreciation of the real effective exchange of the Dalasi at the beginning of the third quarter of 2009, the competitiveness of the Gambian economy may have improved. Other members argued that while this may be true, sustained depreciation of the exchange and the concomitant increase in inflationary pressures is likely to slow economic growth before improving it in the medium to long term when inflationary pressures abate.

(2) Exchange Rate Developments

The global economic and financial crises continue to impact foreign direct investment (FDI), tourism, official aid and remittances. Consequently, the volume of transactions in the foreign exchange market contracted to US$1.2 billion in the year to end-July 2009 from US$1.7 billion a year ago.

Reflecting reduced inflows and an increase in demand, the nominal effective exchange rate of the Dalasi depreciated by 20.8 percent in July 2009 relative to July 2008. Against individual currencies, the Dalasi depreciated by 4.7 percent, 27.9 percent and 18.2 percent against the Pound Sterling, U S Dollar and the Euro respectively.

The Committee indicated that the analysis of the causes of the depreciation of the Dalasi should be more rigorous bearing in mind that the stance of monetary and fiscal policy will have a greater impact on the exchange rate that any other factor given the openness of the Gambian economy.

The Committee members noted that considerable uncertainty surrounds the outlook for the exchange rate of the Dalasi, but expect the currency to be relatively stable in the near term.

(3) Fiscal Developments

Government's fiscal operations in the first half of 2009 deteriorated relative to the same period in 2008. The increase in revenue and grants was offset by the larger than programmed expenditure and net lending.

Revenue and grants rose to D2.2 billion, or 15.5 percent from the corresponding period in 2008. Both tax, non-tax and grants recorded an increase.

Tax revenue rose to D1.8 billion, or by 13.4 percent. Direct taxes declined to D543.9 million, or 8.6 percent largely due to the marked decline in personal taxes from D248.5 million in the first half of 2008 to D230.9 million during the period under review. Indirect taxes, on the other hand, increased to D1.3 billion, or 25.8 percent. Although domestic taxes on goods and services declined to D312.7 million, or 13.5 percent, revenue from international trade surged by 46.8 percent to D992.3 million thanks to the 72.8 percent and 19.1 percent increase in duty and sales tax respectively.

Non-tax revenue and grants rose to D206.0 million and D161.3 million, or 8.9 percent and 63.8 percent respectively.

Expenditure and net lending increased to D2.4 billion, or 20.4 percent. Current expenditure rose D1.64 billion, or 6.3 percent. All the components of current expenditure increased with the exception of other charges.

Capital expenditure and net lending rose to D613.8 million and D159.2 million, or 55.2 percent and 144.3 percent respectively. The bulk of the capital expenditure was financed from Government Local Fund (GLF), which rose to D310.6 million, or 120.6 percent.

The overall budget balance (including grants) on commitment basis widened to D197.7 million, from D86.0 million in the first half of 2008. Excluding grants, the deficit was D359.0 million, higher than the D184.6 million in the corresponding period in 2008.

Both the basic and the primary balance deteriorated from D70.2 million and D454.7 million in the first half of 2008 to negative D3.2 million and D405.7 million respectively during the period under review.

The Committee commented that the annualized budget deficit of 6.0 percent of GDP is a cause for concern and more worrying, was largely financed by the monetary authorities. The huge size of Government borrowing has, in turn, made it difficult to ease monetary policy.

The Committee reiterated the importance of cooperation between the fiscal the monetary authorities to ensure that the policy mix is right and urged that the sources of financing the budget deficit and their magnitude be reflected in report to better inform policy.

The Committee noted the increase in indirect taxes, particularly taxes on international trade. The expected decrease in international trade taxes, owing to the global economic slowdown, did not materialize thanks to strong receipts from oil imports.

The Committee welcomed the review of the tax regime and commented that redistributing income is best achieved not by taxes, but from high and sustained economic growth that trickles down to the entire population.

(4) Money Market Developments

As at end-July 2009, the outstanding debt stock totaled D5.96 billion (29.9 percent of GDP) compared to D6.2 billion in July 2008 (34.5 percent of GDP). The decrease in the debt stock was mainly due to the 37.4 percent and 38.1 percent decline in Non-Interest Bearing Notes (NIB) and the loan to The Gambia National Petroleum Company respectively.

The stock of outstanding Treasury bill, accounting for 83.5 percent of the domestic debt, grew by 1.7 percent from end-July 2008. Commercial banks held 69.6 percent of the stock and the rest was held by the non-bank.

With respect to the maturity structure of Treasury bills, the 364 day bill accounted for 64.98 percent of the stock, 182 day bill (16.49 percent) and the 91 day bill (18.53 percent).

The yield of 91-day, 182-day and 364-day bill decreased to 10.51 percent, 11.29 percent and 13.51 percent in July 2009 from 12.44 percent, 13.6 percent and 15.47 percent respectively in June 2009 attributed to over subscription. The bid-to-cover ratio exceeded 1.

In response to a question on the reason for the reported drop in yield levels of Government securities, it was explained that there has been oversubscription in the market. The Committee then intimated that perhaps this is the time to float more bills so that government reliance on the Central Bank for borrowing would be shifted to the market. The chairman called for consideration of this option within the ambit of the monetary targeting framework, i.e. to the extent that the increase in float does not break the Bank’s monetary targeting benchmarks, it should be pursued. The Committee then called on the Treasury bills committee to be more aggressive in terms of borrowing from the securities market to ensure that Government accounts get funds.

The Committee viewed investors’ preference for longer dated bills as an indication of confidence in the economy. In many advanced countries there has been a flight to shorter-dated securities and even cash given the uncertainty that surrounds the outlook for economic growth.

The Committee noted that the substantial increase in inter-bank placements is an important indicator of the deepening of the banking sector. However, frequent one way borrowing from the market could be a sign of financial distress and hence the need to vigilantly monitor the market.

The Committee indicated that the main source of liquidity in the economy is Government expenditure. As such, liquidity forecasting can be improved if the CBG is provided with good estimates of public sector borrowing requirement over the maintenance period.

(5) Monetary Developments

Money supply grew by 18.0 percent in the year to end-July 2009, compared to 10.1 percent a year earlier. This was mainly on account of the 32.3 percent growth in the net domestic assets (NDA), off-setting the 3.4 percent contraction in the net foreign assets (NFA) of the banking system.

Narrow money, which comprised currency outside banks and demand deposits, grew by 12.5 percent. Demand deposits rose by 13.8 percent and currency outside banks by 10.1 percent. The ratio of narrow money to broad money fell from 49.5 percent in July 2008 to 47.2 percent in July 2009.

Quasi money, which comprised savings and time deposits, increased by a robust 23.4 percent from July 2008. Savings and time deposits grew by 12.9 percent and 39.1 percent respectively.

Reserve money grew marginally by 1.8 percent, relative to 6.8 percent in July 2008. The NFA and the NDA of the CBG rose by 2.9 percent and 42.6 percent respectively.

The Committee expressed concern about the high growth in money supply and the increasing claims on Government net by the Central Bank.

Some Committee members observed that there is a seeming inconsistency and disconnect between the robust growth in money supply and the deceleration in inflationary pressures. The overwhelming sentiment was that inflation is a lagged variable and as a result, the decline in general prices may be as a consequence of modest growth in money supply in the past and the slowdown in global economic activity.

(6) Financial Stability Report

According to the most recent data, the capital and reserves of the banking system increased to D1.58 billion in June 2009, or 8.1 percent from June 2008. The risk weighted capital adequacy ratio averaged 33.9 percent, higher that 30.8 percent in June 2008. All the banks observed the minimum requirement of 8.0 percent.

Total assets increased to D13.3 billion, or 18.2 percent partly reflecting the 30.1 percent growth in loans and advances. Lending to all the sectors increased with the exception of tourism which contracted by 17.9 percent. The non-performing loans (NPL) ratio at 7.0 percent in June 2009 was unchanged relative to March 2009 reflecting in part to a tightening of credit standards.

Deposit liabilities continue to expand at a strong pace and totaled D8.5 billion in June 2009, or an increase of 22.2 percent from a year ago. Earnings also increased. Net income rose from D45.0 million in the first quarter to D54.0 million in the second quarter of 2009. The return on assets and return on equity was 1.64 percent and 3.56 percent respectively in June 2009.

The Committee requested that in the future, the analysis should be expanded to include the distribution of non-performing loans by sector, the share of loans to total assets, the level of contingent liabilities, stock of foreign currency deposits and the breakdown of the growth/contraction of capital and reserves as well as other important soundness indicators.

The Committee members noted that the increase in capital and reserves was explained by both capital injection and growth in reserves. Regarding the possibility of setting a higher capital adequacy ratio for new banks, the overwhelming sentiment was that it may not serve the intended purpose given that the new banks, with a small asset base, would not have difficulties in meeting the requirement.

The Committee commented that based on soundness indicators, banks in The Gambia are sound and that the banking crisis in Nigeria had little or no impact on their subsidiaries in The Gambia. The Committee members, however, advised on the need to be vigilant bearing in mind that a bad bank anywhere can affect a good bank everywhere.

(7) Real Sector Developments

Economic growth is projected to moderate to 3.6 percent in 2009 compared to 6.1 percent in 2008 attributed principally to the slowdown in global economic activity and the attendant decline in FDI, remittance and tourism flows.

The Committee members indicated that considerable uncertainty surrounds the outlook for economic growth, but see the risks around the outlook as skewed to the upside should the plentiful and well distributed rainfall is sustained.

The Committee indicated that the key to expanding the economy and reducing poverty is to increase investment in agriculture and lauded the Government's renewed impetus to scale up investment in the sector to boost production and productivity.

(8) Business Sentiment Survey

Readings of the most recent business sentiment survey revealed that 64 percent of respondents think that overall economic activity in the second quarter would be unchanged relative to the first quarter. At the company level, 73 percent of respondents indicated that activity was higher in the second quarter relative to the first quarter. Most respondents were of the view that activity at both the business and country level would be higher in the third quarter compared to the second quarter.

The majority of respondents (60.0 percent) indicated that capital expenditure was higher in the second quarter relative to the first quarter. Inflationary expectations were unchanged, with the majority of respondents indicating that general prices are expected to be the same as in the second quarter.

The Committee noted that the trend decrease in general prices partly caused inflationary expectations to remain well anchored, but emphasized the importance of monitoring inflation developments carefully.

(9) Inflation

According to the readings of the National Consumer Price Index, end-period inflation increased to 4.1 percent in July 2009, slightly higher than the 3.7 percent recorded a year earlier. Average inflation rate accelerated to 6.1 percent from 3.3 percent in July 2008.

Food price inflation decreased to 4.3 percent in July 2009 relative to 5.1 percent in July last year. Non-food prices, on the other hand, increased to 3.8 percent from 2.5 percent in July 2008.

Core Inflation, which excludes the prices of energy and volatile food items, rose from 3.1 percent in July 2008 to 4.6 percent in July 2009.

Month-on-month, all key measures of inflation registered steady declines during the firs seven months of the year. Headline inflation declined from 6.83 percent as at the end of the first quarter, to 5.35 percent at the end of the second quarter and further inched down to 4.11 percent as at end July 2009. Core inflation followed a similar trend, declining from 5.49 percent as at the end of the second quarter, to 4.63 percent as at end-July.

The Committee commented that the subdued inflationary pressure is partly the result of the prudent policy responses of monetary and fiscal authorities and partly the decline in global commodity prices.

Taking into account the deceleration in inflationary pressures and the benign outlook, the Monetary Policy Committee decided to maintain the rediscount rate, the policy rate, at 16.0 percent.