POLICY STATEMENT 2010

Consolidating Gains and Charting New Directions:
A Strong Financial System for Sustainable Economic Growth

I. INTRODUCTION

This Policy Statement sets out the fundamental objectives of monetary policy and goals of the Central Bank of Liberia (CBL) relative to the development, regulation and supervision of the nation's financial system for the current year. The basic message is two-fold: consolidation of gains emanating from the reforms in the past few years and using the strengthened position of the Bank to chart new directions as a means to becoming more effective in maintaining a stable macroeconomic environment and supporting stronger economic growth underpinned by a more dynamic private sector.

The Bank's transition to the use of the International Financial Reporting Standards (IFRS), which has been the basis for the auditing of its financial statements since end-2008, and the bi-annual Safeguard Assessment audits have underpinned the commitment of the Board of Governors to transparency and accountability. These audits are conducted by the Bank's external auditors, PriceWaterhouseCoopers, and are made available to the Government through the President. They are also provided to the IMF in the context of the program that Liberia has with that institution. The CBL audits are posted on its website for the general public. The external auditors concluded that the financial statements for 2009 give a true and fair view of the financial position of the Central Bank and its cash flow in accordance with International Financial Reporting Standards. The external auditors also noted that internal controls of the Bank were operating in a regular fashion.

The CBL has stepped up its communication with the public with the introduction of the CBL's Newsletter, a bi-monthly publication. This is in addition to the Monthly Fact Sheet, the bi-monthly Statistical Bulletin and the Quarterly Economic Bulletin. The Bank also calls press conferences, as may be necessary. The Bank believes that public expectations are more likely to help foster economic stability when the public has a clear understanding of what the Bank's goals are; how it views developments in the economy; and how it is likely to respond to various economic circumstances. The CBL will continue to find ways of enhancing its public outreach, while ensuring the continuation of regular consultations with the fiscal authority, the commercial banks and other key stakeholders. Also, the CBL will continue to work cooperatively with its international partners, including the IMF, the World Bank, the African Development Bank (AfDB), and the West African Monetary Zone (WAMZ).

II. THE DOMESTIC ECONOMY

The Liberian economy was negatively impacted by the global financial crisis and economic meltdown through a number of channels, including job losses in the export sector, slowdown in foreign direct investment and inflows of workers' remittances, and the weakening of the exchange rate. However, the economy grew by about 4.6 percent in 2009, compared with the 1.5 percent average growth rate for Sub-Saharan Africa. Progress is being made towards reviving iron ore mining; rubber exports have stabilized; two major concessions have been granted for oil palm development, and construction is on the rise. The continuation of sound fiscal and monetary policies in 2009, despite the difficult external environment, coupled with governance reform, also placed the economy in a better position for rebound in 2010. GDP in 2010 is expected to grow between 6-7 percent. However, it is important to deal with the infrastructure deficit through a well-defined medium to longer-term public investment program and to enhance measures aimed at raising agricultural productivity. Medium-term growth has to also be underpinned by Liberian small and medium sized enterprises.

The average rate of inflation in 2009 was 7.4 percent, down from 17.5 percent in 2008, largely reflecting the domestic pass-through effects of the relatively low oil and food prices on the world market. Domestic food inflation at end of the first quarter of 2010 was 6.4 percent, compared with negative 3.6 percent for the first quarter of 2009. Main drivers for the domestic food inflation include transportation cost for bringing food items to the market, exportation of some locally produced food items to neighboring countries which leads to scarcity of such commodities on the local market, and low production of a number of domestic food items due to seasonality.

Inflation outlook in 2010 will largely be dependent on movements in the prices of oil and food on the international market and the continuation of broad exchange rate stability. While the level of inflation will be influenced by exchange rate developments, a number of structural problems will also have an impact; namely, conditions at the Freeport of Monrovia, the poor state of farm-to-market roads, and the high cost of electricity. Since the beginning of the year, the rise in domestic food prices has begun to put upward pressure on inflation, suggesting the need to maintain the focus on domestic food production and to improve the access of farmers to markets at reduced costs.

Regarding the banking sector, the minimum capital requirement was increased to US$8.0 million at end-December, 2009, from US$6.0 million at end-December 2008. The balance sheet of the banking sector expanded in all key areas, and there was improvement in key prudential ratios. There was also improvement in corporate governance, risk management practices, and internal controls.

The number of commercial banks increased from 6 to 8, with the starting of operations of AccessBank Liberia Limited (ABLL) — the Microfinance Bank, and Guaranty Trust Bank Liberia Limited (GTBLL). Branch banking network also increased further, from 28 branches as at end-December 2008 to 55 in 2009. The licensing of AccessBank, with its focus on microfinance, was in keeping with the CBL's objective of improving access to financial services by those with low-income and the economically active poor.

The banking sector continued to make a significant contribution to the recovery of the economy. Total credit to various sectors of the economy increased by 54.0 percent to L$9,568.7 million at end-December, 2009, from L$6,227.8 million at end-December, 2008. The US-dollar share of total credit increased from US$89.2 million in 2008 to US$125.7 million, while the Liberian-dollar share rose from L$519.2 million to L$708.9 million during the same period.

Money supply (M1), comprising Liberian dollars only, rose by about 14.0 percent to L$5,030.1 million at end of 2009, from L$4,413.0 million at end of 2008, slower than the 21.6 percent growth between 2007 and 2008. Broad money (M2), comprising both Liberian dollars and US dollars (converted to Liberian dollars), grew by 43.1 percent to L$24,235.3 million at end-December 2009, from L$16,931.0 million at end-December 2008. The US dollar component accounted for L$17,835.0 million or 73.6 percent at end of 2009, while the Liberian dollar share was L$6,400.3 million or 26.4 percent.

The Liberian dollar exchange rate came under pressure during 2009, depreciating by 10.2 percent, from L$64.00/US$1.00 at end-December, 2008 to L$70.50/US$1.00 at end-December, 2009. This was due largely to the global financial and economic crisis, which led to a reduction in the supply of US dollars to the economy, including through the slowdown in workers' remittance inflows to Liberia and the decline in export earnings.

The trade deficit for 2009 amounted to US$396.1 million, 30.7 percent lower compared with US$517.7 million for 2008. However, this narrowing was mainly the result of lower imports. In the circumstances, the need to raise production for exports cannot be overemphasized.

III. POLICY IMPLEMENTATION: 2009

The weekly foreign exchange auction remained the key policy instrument for affecting domestic monetary condition, with increased intervention by the CBL in the foreign exchange market to help ease the pressure on the exchange rate of the Liberian dollar. The CBL sold a total of US$36.1 million through the auction, US$10.1 million more than what was sold in 2008. This took place while the CBL continued its policy of reserves accumulation.

Among the decisions taken by the Board of the CBL were the following:

- approval of the commencement of work on developing a Treasury bill (T-bill) market;
- adoption of the Risk-Based Supervision (RBS) approach to replace the current Compliance-Based Supervision Approach;
- increasing the Single Obligor Limit for credit extension to any borrower by a commercial bank from 15.0 percent to 20.0 percent of its net worth;
- adoption of an investment strategy to maximize income to the Bank, and establishment of a Board Investment Committee;
- granting of a Provisional License to First Afriland Asian American Bank in line with CBL's policy to expand and diversify the banking sector and in recognition of the commitment of this institution to direct a significant share of its resources towards agricultural financing;
- supporting the establishment of a Banking Institute in collaboration with the Liberia Bankers Association to be housed at the CBL Training Center in order to help build capacity within the banking sector;
- agreeing that the CBL should assume a leading role in developing a capital market;
- supporting the establishment of a fast-track court for the expeditious enforcement of commercial contracts as a means of improving the credit environment;
- approval of a Regulatory and Supervisory Framework for Microfinance.

The CBL also took several specific actions aimed at protecting the stability of the banking sector:

- a memorandum of understanding was agreed with the Central Bank of Nigeria for the sharing of supervisory information, including actions taken regarding crisis management relating to Liberian subsidiaries and their parent banks in Nigeria;
- a new Guideline for the Management of Foreign Exchange Risk Exposures and Placements Abroad by banks –No.CBL/SD/004/2009– was issued, intended to mitigate the potential foreign exchange and liquidity risks arising from commercial banks' US Dollar exposures, including their placements abroad;
- a Guideline Concerning Supervisory Intervention –No.CBL/SD/005/2009– was issued, aimed at ensuring timely and transparent supervisory interventions in banks showing weaknesses that threaten their safety and soundness;
- a directive on the introduction of financial products and services for commercial banks – No.CBL/SD/001/2009– was issued to guide commercial banks in the launching of new financial products or services, taking due account of the need to protect consumers and ensuring that such new financial products do not expose the banking system to abuse by money launderers. It should be noted that new financial products introduced in 2009 by commercial banks included ATMs, debit cards, visa cards and other proprietary products.
- commercial banks were advised through directive – No.CBL/SD/002/2009– on procedures for the expansion and closure of bank branches;
- a new Guideline –No.CBL/SD/003/2009– for the Management of the Credit Reference System at the CBL was developed in order to enhance the sharing of information on the credit history of potential borrowers.

Meanwhile, the CBL continued its supervisory strategy of a robust inspection of banks, which involved conducting two comprehensive on-site examinations of each bank during the year. This was complemented by a vigilant off-site surveillance and follow-up examinations.

III. POLICY DIRECTION FOR 2010

A. MONETARY POLICY

It is important to focus on monitoring liquidity to help ensure that money supply is consistent with a stable macroeconomic environment. Accordingly, steps are being taken to strengthen capacity in the areas of liquidity monitoring and forecasting. Essentially, reserve requirements, the foreign exchange auction and the T-bill auction, for which modalities are to be finalized by end-June 2010, will be the CBL's main tools for monetary policy operations. It should also be noted that the T-bill market will help the government to raise Liberian dollars and provide investment opportunities for excess Liberian dollar liquidity. The T-bill market will also help to make interest rates a viable tool for monetary policy. The CBL will participate in the market with non-competitive bids for monetary management purposes and will also participate in the secondary market to buy T-bills from banks at its discretion to be able to supply liquidity to a bank short of liquidity.

For the 2010/2011 fiscal year, the CBL is prepared in the event of a temporary delay in external budget support or ratified concession signature payments to extend short-term credits to the government up to an agreed ceiling at mutually acceptable terms.

The CBL is taking steps to spearhead the orderly development of a capital market in Liberia, which will be one of the responsibilities of a newly formed Treasury Operations Unit in the Bank. Early this year, the CBL invited a consultant to conduct an assessment with CBL officials and meet with key stakeholders on capital market development. Consultations will be held with other experts as well. During the course of this year, the CBL will focus on developing an interim regulatory framework, and prepare a road map for the development of a full-fledged capital market.

The CBL will continue to promote a wider use of the Liberian dollar in 2010. Improving the quality of bank notes in circulation should assist this effort. Notwithstanding, the public should be aware that there is a cost associated with withdrawing mutilated banknotes and replacing them with new ones.

The reserve position of the CBL has improved considerably as a result of the Special Drawing Rights (SDRs) allocation, and the CBL will continue with efforts aimed at promoting de-dollarization that could further enhance reserve adequacy and improve its income.

B. THE FINANCIAL SYSTEM

The key policy objectives of the CBL relating to financial system reform include the following:

1. STRENGTHENING THE REGULATORY AND SUPERVISORY REGIME

(i) The CBL will begin the implementation of the Risk-Based Supervisory Framework during the second half of 2010, which is a change from the traditional compliance-based supervisory framework. To this end, staff of the CBL recently completed training programs at the Bank of Uganda, Bank of Tanzania and the Reserve Bank of Zimbabwe. The CBL is receiving technical assistance from the IMF to help carry out this program.

(ii) Given the improvement in the risk management practices and corporate governance in the banking sector, coupled with the implementation of risk-based supervision, the CBL will revert to once-yearly on-site examination. However, banks showing severe weaknesses in certain areas will be subjected to more aggressive follow-up examinations.

(iii) All commercial banks will be required to be in compliance with the International Financial Reporting Standards (IFRS) by end-December 2012. The CBL will develop a framework to guide the transition process and support efforts toward building the capacity of the banking sector to ensure a successful transition. The implementation of IFRS by commercial banks will promote transparency and market discipline in the financial sector.

2. PROMOTING MEDIUM TO LONG-TERM LENDING TO STRATEGIC SECTORS OF THE ECONOMY

Although aggregate credit to the private sector has been rising, agriculture and manufacturing accounted for only 3.4 percent and 1.7 percent at end-December 2009, respectively. Financing of these sectors is critical to supporting job creation, economic growth, and improving the balance of payments of the country. In March, a credit guarantee scheme was launched at the CBL supported by USAID through its Development Credit Agency to share the risk for commercial banks lending to agriculture and SMEs, a welcome move that should help increase the allocation of credit to these sectors. It is important to note that the success of such a scheme depends to a large extent on borrowers taking responsibility to repay. Also, the CBL has received commitment from the bank that received a provisional license earlier this year to direct a significant portion of its lending to agriculture. This was an important factor in the CBL's decision to grant the bank a provisional license. The CBL will continue to explore ways of identifying potential sources of funding to stimulate private sector investment, not just in Montserrado and its environs, but throughout the country.

Efforts to mobilize resources to fund the private sector should also be supported by reasonable lending rates and appropriate maturity structures. The CBL expects to have a constructive engagement with the commercial banks to address these issues in a concrete way in the near term. Finding ways to enhance intermediation must be a priority of the commercial banks. The CBL will work with commercial banks to achieve material progress in a reasonable time. There will also be engagement with commercial banks regarding their collateral requirements for lending to start-up businesses, many of which continue to find it difficult to meet such requirements. In this regard, the CBL will encourage the banks to develop innovative ways to address this situation without compromising the principles of sound risk management practices.

3. IMPROVING THE CREDIT CULTURE

The CBL will continue to work with the Liberia Bankers Association (LBA) and the Liberia Bar Association (LBA) to bring the idea of establishing a fast-track commercial court to fruition this year. Experts have been hired with financing from the IFC to draft the law and operational procedures for this court, and a fact-finding tour by key stakeholders has been made to Ghana to get information on the workings of such a court in that country. In addition, the CBL will support alternative approaches being considered by the commercial banks aimed at improving collection of non-performing loans, including the publication of the names of serious delinquent borrowers. What the public should be aware of is that money borrowed from banks that is not repaid is the public's money deposited in the banks.

The current credit reference system at the CBL will be improved as a means of enhancing information sharing on the credit history of prospective borrowers. However, it is important to clarify that the final credit decision and/or credit assessment of a borrower is the sole responsibility of individual banks. The medium-term goal of the CBL is to have a privately-managed credit reference bureau. To this end, the Bank will finalize work on the legal and regulatory framework for the establishment of a privately-managed credit reference bureau during the course of the year.

4. EXPANDING THE FINANCIAL SYSTEM

With 8 banks operating in the country and the expectation of an additional one around mid-2010, the CBL will give consideration to licensing only institutions that are oriented towards meeting strategic needs of the economy such as agriculture, housing, and microfinance. The granting of new licenses to failed banks is not under consideration as part of the expansion program. This is important to avoid undermining confidence in the banking system as a result of the negative perception associated with failed banks and non-bank financial institutions.

The expansion of banking services to all parts of the country, especially to counties that are underserved or have no bank branches, will be encouraged. However, this will take into account the managerial and financial capacities of individual banking institutions and the risk of over-concentration of branches in one location. The CBL will also be guarded against the over extension of individual banks such that they become "too big to fail", with potentially serious consequences for the economy.

Regarding non-bank financial institutions (NBFIs), the CBL will conclude work in the first half of 2010 on an appropriate regulatory framework, for implementation immediately thereafter. Consideration of applications of NBFIs will be given to those that demonstrate the capacity to add value to the financial sector based on realistic and credible business plans. The CBL will work towards finalizing the regulatory framework for lease financing, which is expected to spur the development of this sector.

Further steps will be taken to mainstream the activities of the foreign exchange bureau, working in cooperation with the leadership of the Association of Foreign Exchange Bureaus. Among other things, the CBL intends to strengthen supervision over the operations of foreign exchange bureaus, develop a reporting format for them, and encourage steps aimed at bringing these institutions more into the formal economy. The CBL will also work with the leadership of the Association to build consensus on the need for encouraging merger among significantly important foreign exchange bureaus or operators.

5. SUPERVISING THE INSURANCE INDUSTRY

In the recent past, the CBL has been building capacity to regulate and supervise the insurance industry in keeping with its mandate under the New Financial Institutions Act of 1999. It is important to move the process forward, as the insurance industry has the potential to be an important part of the financial sector. Accordingly, the CBL will actively engage the relevant stakeholders to remove any misunderstandings with regard to its legal mandate regarding the supervision and regulation of the insurance industry in Liberia. The Bank will also work towards the devolution of the regulation and supervision of the sector to an autonomous agency in due course.

C. PAYMENTS SYSTEM MODERNIZATION

The CBL is presently working with the West African Monetary Institute (WAMI) on the modernization of Liberia’s payments system. A project has been developed, which is expected to begin in October, 2010, with financial assistance largely from the African Development Bank. Modernization of the payments system will promote financial deepening and stability, and facilitate more efficient cash management. Key components of the project include:

- Real Time Gross Settlement (RTGS) system for inter-bank, urgent and large funds transfer;

- Automated Clearing House (ACH) and Automated Cheque Processing (ACP) system to promote electronic transactions and cheque truncation, with a view to reducing the clearing cycle to international best practice and engendering public confidence in the use of non-cash payments.

- Scriptless Securities Settlement (SSS) system to deepen the money market, which is currently shallow and rudimentary.

- Core Banking Application (CBA) to ensure an efficient service delivery to customers by the Central Bank.

- Infrastructure upgrade, Local Area Network (LAN), Metropolitan Area Network (MAN) etc., which is a pre-requisite for the installation of RTGS, ACH, ACP, SSS and CBA.

- Automated Teller Machine (ATM) or Point of Sale (POS) switches to promote electronic transactions and reduce the amount of currency outside the banking system.

- Electronic-Financial Analysis and Surveillance System (E-FASS) to facilitate efficient banking system supervision.

In order to reduce the vulnerability of GoL checks to fraud, the CBL has commenced printing checks through internationally accredited check printing companies. Additionally, as part of its effort to provide the Ministry of Finance, Government agencies and commercial banks with timely accounts information, e-statement services has been launched.

In another development, the request from an operating commercial bank in Liberia to provide mobile money services to the general public has been approved. The CBL is encouraging the expansion of such services to ease payments in rural areas.

D. ENHANCING ACCESS TO FINANCIAL SERVICES BY THE POOR AND LOW INCOME GROUPS

During 2010, the CBL will take further steps to enhance the provision of microfinance services in a more diversified and sustainable way for poor and low income groups. Already, a Microfinance Regulatory and supervisory Framework for Liberia has been issued earlier this year, which will, amongst others, provide appropriate means for tracking the activities of development partners in the microfinance industry.

Steps are being taken to commence Phase II of the “Launch of an Inclusive Financial Sector in Liberia (LIFS).’’ It will be recalled that Phase I of the project contributed on-lending funds to two microfinance institutions (MFIs) as grants; completed the regulatory and supervisory framework of MFIs; initiated the foundation course in microfinance for practitioners, and established the microfinance network. The second phase will support the development of a sustainable inclusive sector through three levels:

> At the micro level, it will focus on building sustainable financial services providers via capacity building and expansion for microfinance institutions; development of innovation in rural finance, savings services and electronic banking applications; improvement of microfinance institutions and other financial services providers access to loans and/or grants for on-lending to clients; improvement of rural women access to sustainable microfinance services to support their engagement in economic activities; and development of client focused financial products such as loan, savings and other financial products.
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> At the middle level, the project will strive to establish supportive infrastructure by means of support to Liberia Microfinance Network, the University of Liberia and Cuttington University.
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> At the macro level, emphasis will be on strengthening the technical and operational capacity of the CBL.

In concert with its international partners, the CBL will seek to expand the provision of financial services at the community level through the Village Savings and Loan Association (VSLA) Initiative. Already in 2010, six (6) such associations have been established in three (3) counties; namely, Cape Mount, Sinoe and Maryland.