CENTRAL BANK OF LIBERIA

POLICY STATEMENT 2012

I. OVERVIEW

In the past few years, the Central Bank of Liberia has endeavored to transform the Liberian financial landscape and maintain macroeconomic stability. This has entailed enhancing the soundness of the financial system, improving access to financial services, and taking steps to ensure a relatively stable exchange rate, while strengthening the reserve position of the Bank. Additionally, the Bank has expanded its outreach to Liberian small- and medium-scale enterprises with a view to supporting broad-based economic growth.

The policy direction for 2012 will continue on the path of reform, grounded in the following objectives: promoting profitability of the banking system, with emphasis on further improving the credit environment and reducing the level of non-performing loans; strengthening the capability of the CBL to more effectively conduct monetary policy, including establishing a policy framework for addressing the question of the dual currency regime in the medium term; strengthening the CBL's regulatory and supervisory capacity; stepping up work towards the deepening of the financial system; supporting increased access to credit for the Liberian private sector; continuing the expansion of banking services to the low-income population and to underserved areas; enhancing consumer protection; and consolidating the renewed confidence in the banking system.

II. RECENT ECONOMIC DEVELOPMENTS

Prospects for global economic recovery are improving, but with expected weak growth in the euro area and high unemployment in many advanced economies. According to the IMF April 2012 World Economic Outlook (WEO), global growth is projected at 3.5 percent in 2012, down from 3.9 percent in 2011. The slowdown is mainly on account of the expected recession in the euro area with growth declining to a negative rate of 0.3 percent, from 1.4 percent in 2011. The US economy is projected to grow at 2.1 percent in 2012, from 1.7 percent in the preceding year. Asia is expected to grow at 6.0 percent, roughly the same level in 2011, though with considerable regional variations, with China and India leading with growth at about 7.0 percent. Growth in Sub-Saharan Africa is projected at 5.4 percent, 0.3 percentage point more than the 5.1 percent level in 2011. Inflationary pressure is easing in the major advanced and emerging market economies, with inflation expected to slow at 1.9 percent and 6.2 percent in 2012, from 2.7 percent and 7.1 percent in 2011, respectively. On the other hand, inflation for Sub-Saharan Africa is expected to remain high due to accommodative macroeconomic policies and supply-side constraints.

On the domestic front, real GDP is estimated to grow at 8.8 percent in 2012, higher than the 6.9 percent recorded for 2011. This growth will largely be driven by activities in the agricultural and the services sectors and the resumption of iron ore exports. However, uncertainty in the global economy has implications for remittances, investment, foreign aid, and demand for primary commodity exports. In 2011, domestic inflation averaged 8.5 percent, compared with 7.5 percent in 2010, driven by the pass-through effect of international fuel prices and domestic food inflation. The major risk to maintaining single-digit inflation in 2012 remains the persistent high global price of oil, poor farm-to-market roads and the current monetary situation that needs close monitoring. Liberia has experienced a relatively low inflationary and stable exchange rate environment relative to almost all the countries in the ECOWAS region. Between January and December 2011, the Liberian dollar experienced the lowest rate of depreciation among the countries of the West African Monetary Zone (WAMZ), depreciating by 0.7 percent, from L$72.00/US$1.00 in January 2011 to L$72.50/US$1.00 at end-December 2011. The region averaged a rate of depreciation of 6.4 percent.

The value of exports and imports stood at US$367.0 million and US$1,033.7 million at end of 2011, respectively, resulting in a trade deficit of US$666.7 million, up from US$487.8 million in 2010. Imports are mainly financed through foreign direct investment, accounting for about 90.0 percent of current account financing; a situation that will continue in the current year.

The banking sector recorded steady growth last year and continues to be well capitalized and liquid. However, the sector remains challenged by the high level of non-performing loans (NPLs), although it declined to 20.8 percent at end-December 2011, from 25.1 percent at end-December 2010. Credit to the private sector increased to L$16,170.3 million, compared with L$12,623.5 million at end-December 2010. Money Supply (M1) at end-December 2011 amounted to L$30,069.6 million, from L$ 23,212.7 million at end-December 2010, driven by a 33.9 percent increase in currency outside banks and 28.3 percent rise in demand deposits. Broad money (M2) or overall liquidity grew by 39.5 percent between December 2010 and December 2011.

Macroeconomic Challenges

The lack of diversification remains a major issue, and the high dependence on foreign investment mainly in the enclave sector, which is the major source of financing for the current account, is not sustainable. A more rapid decline in unemployment and poverty will require more broad-base economic growth. Against this background, it is important that policies remain focused on increasing productivity in the real sector of the economy aiming at both the domestic and export markets. Cheaper power and better road and port facilities will be critical. The growing demand for foreign exchange is beginning to put pressure on the exchange rate; hence, the importance of CBL having additional tools to manage liquidity. In the financial sector, there is weak credit to agriculture. Also, the system is faced with low availability of long-term funding for investment, including for housing. This is why further steps towards broadening the financial market are essential. Regarding the budget, the shift to a medium-term framework will require discipline, especially with regard to channeling more resources to the capital budget. All in all, bold, consistent decisions must be taken with a view to transforming the structure of the economy over time.

III. KEY POLICY DECISIONS: 2011

The CBL continued the foreign exchange auction in 2011 as the major policy tool to influence domestic liquidity. A total of US$39.2 million was sold in 2011, compared with US$44.1 million in 2010, representing a reduction of 11.2 percent. The reduction was partly due to broad exchange rate stability and increased remittance inflow in 2011 relative to 2010.

Among the key decisions of the Board of Governors in 2011, were the following:

- approval of the implementation of measures aimed at reforming the operations of foreign exchange bureaus based on the following 3 key objectives: (1) encouraging mergers and consolidation to create larger and sustainable foreign exchange bureaus; (2) modernizing operations and activities of foreign exchange business; and (3) reforming the Association of Foreign Exchange Operators to ensure wider representation;
- approval of the Interim Regulations for Non-Bank Financial Institutions ;
- endorsement of the establishment of a Consumer Protection Unit within the Regulation and Supervision Department to focus on ensuring that customers are protected against unfair or unethical practices by financial service providers, and that applicable regulations are adhered to;
- amendment of the Regulation Concerning Banking License to make it more comprehensive and relevant in keeping with contemporary international standards, including the Basel Core Principles;
- removal of the monopoly clauses in agreements between banks and money transfer organizations;
- authorization for the development of a framework for the issuance of CBL Notes.
- resolution to complete the CBL’s Headquarters on Ashmun Street as a necessary step to enable the Bank to have a suitable accommodation to carry out its statutory functions, including the conduct of a more effective monetary policy.

IV. POLICY DIRECTION FOR 2012

MONETARY POLICY

The thrust of monetary policy in 2012 and over the medium-term will be focused on containing inflation, but emphasis will also be on ensuring growth that is supportive of economic development, job creation and poverty reduction. At the moment, efforts are being exerted to widen the scope of policy instruments available to the CBL to enhance the conduct of monetary policy, including urging the Government to introduce the Treasury-bill market as proposed by the CBL a year ago. The issuance of CBL Notes, remains an option should it become necessary.

Against the backdrop of the debate on the dual currency that has become a topical issue in recent months, especially in the ongoing **Liberia Rising 2030** nationwide consultative meetings, it should be noted that the CBL, well before now, has been considering the matter internally as part of its efforts to improve macroeconomic management. The decision for Liberia to join the West African Monetary Zone (WAMZ) in February of 2010 is a clear indication that the dual currency regime is not sacrosanct. In any event, the process of change must be handled with a sound understanding of economic fundamentals, which calls for a strategic approach in the context of a medium-term timeline so as to leverage the stable macroeconomic conditions that have been part of Liberia's economic landscape in recent years. Going forward, the path of dedollarization must be supported by a well organized and realistic development program of Government aimed at strengthening productivity within the real sector, enhancing production for both exports and local consumption, as the foundation for the Liberian dollar being a store of value. With a consensus built around a medium-term time-frame, the monetary and fiscal authorities and other strategic institutions have to work in tandem such that monetary, fiscal and structural policies are seen as being supportive of a greater use of the Liberian dollar in order to ensure a soft landing for the economy. It is important to stress that currency exchange and convertibility will remain free and market-driven, and the transition will be orderly. The CBL's policy of limiting excess volatility of the Liberian dollar will continue. Meanwhile, the CBL is taking steps to strengthen its capacity for more robust monetary policy management that a single currency regime will require. It should also be noted that the regular use of the Liberian coins will be part of the dedollarization exercise. This will help to facilitate small transactions in the economy, support price stability and enhance utility associated with money income. Accordingly, steps are being taking by the CBL to ensure an adequate supply of coins in L$1 and L$0.50 denominations.

Although this will entail the loss of seignorage to the CBL, it has been considered that the benefit to the public should outweigh such loss. Minting coins in lower denominations does not appear to be economically justifiable at this time. Higher denomination Liberian dollar banknotes will also be part of the transition process to facilitate higher value transactions. The public will be appropriately informed of developments regarding this matter.

THE FINANCIAL SYSTEM - Enhancing the Profitability of the Banking System

As mentioned earlier, the banking system is challenged by low profitability, largely on account of provisions for non-performing loans (NPLs). This situation has the potential of undermining the stability of the system and the larger economy. The profitability question will be handled through a multifaceted approach:

- the CBL will continue to work with other stakeholders in providing the necessary support for the effective functioning of the newly established Commercial Court.

  In addition, the CBL will apply resources towards establishing a collateral registry in the country, as a necessary step in supporting the work of the Commercial Court and protecting the security interests of commercial banks. The collateral registry will facilitate the timely verification of collaterals and foreclosure proceeding on collaterals in a more cost-effective manner.

- the CBL will begin immediately a review of the relationship between delinquent borrowers of respective banks, including corporate entities, to implement a policy of naming and shaming. The CBL will also issue a directive that will bar the banks from dealing with major offenders, including prohibiting the opening and/or maintenance of accounts and the transfer of money out of Liberia on behalf of such offenders.

- CBL will encourage syndication among banks to facilitate the financing of large-volume transactions with good returns.

- CBL will engage the fiscal authority to consider financing options involving the commercial banks for key public projects, as a means of providing additional avenues for banks to invest some of their excess liquidity. There is added advantage of the Government drawing on local resources to help carry out its investment program to boost growth and develop the private sector. The timely roll out of the Treasury bill program will also contribute to strengthening the balance sheet of the commercial banks. Steps will be taken to ensure that there is no crowding out of lending to the private sector.

In addition to the above, the CBL intends to enhance the existing Credit Reference System (CRS), which has played a very important role in facilitating the sharing of credit information among the banks, and, to some extent, helped to contain the rise in non-performing loans. The Bank will also continue with its initiative toward the establishment of a full-fledged credit reference bureau, as a medium- to long-term goal.

Meanwhile, the efforts by the CBL to tighten support against fraud and theft in the banking system need to be complemented by the Government in ensuring a stronger system for bonds provided by accused persons from owners of real properties and insurance companies, with a view to ensuring that instruments provided are credible.

Strengthening Regulatory and Supervisory Capacity

The Bank will continue to strengthen the capacity of the Regulation & Supervision Department in critical skills such as risk-based supervision, information technology examination, and international financial reporting standards.

Work has begun towards developing a framework for stress testing and conducting macro-prudential analysis of the banking sector as part of efforts to strengthen early warning tools and addressing issues of systemic risk on a more proactive and timely basis.

Promoting Financial Inclusion

Access to financial services by a large segment of the population is a key factor in ensuring balanced growth and development. In this regard, the CBL is committed to supporting the establishment of specialized rural/community financial institutions in collaboration with interested banks. These institutions will be owned by the local people themselves and should help in the mobilization of local savings while providing financial services to the respective communities. Also, the CBL has begun working with the credit union movement in the country, leading to the hosting of a national congress for credit unions in Zwedru, Grand Gedeh County in April 2012. At this congress, the internal governance policies and procedures of the Liberia Credit Union National Association (LCUNA) were revised and adopted. Meanwhile, the Bank has negotiated a grant of US$500,000 from UNCDF global program and funding from the ACP/EU Microfinance Program through the Irish League of Credit Unions to be used for technical assistance to strengthen credit unions in Liberia.

The CBL will continue to work with development partners to expand the village savings and loan association scheme throughout the country.

Strengthening Consumer Protection

The CBL is taking further steps to strengthen the capacity of the Consumer Protection Unit (CPU) for its effective functioning. The CPU was established in 2011 as part the Bank's Regulation and Supervision Department. It is important that the public cooperate with the CBL for the effective functioning of the unit by properly channeling complaints to the Unit, which is mandated to protect consumers against unfair and unethical banking practices.

Supporting Increased Access to Credit for the Liberian Private Sector

It is important that support for Liberian entrepreneurship be a central part of the new socio-economic dispensation, and the CBL will continue to do what it can within the confines of its resources to contribute to this endeavor. The Credit Stimulus Initiative, which was launched in December 2010, has yielded encouraging results. Under the program, US$5.0 million was made available for on-lending to Liberian-owned businesses in various areas of operations such as transportation, services, manufacturing, gas and oil, agriculture, fisheries, retail and woodwork. By end-April 2012, some 52 Liberian-owned businesses covering about 11 sectors of the economy and employing about 2,608 individuals had benefitted from the Program. Under this scheme, the cap placed on interest rate was 8.0 percent, but the average interest rate at which these businesses were able to borrow had been around 6.0 percent.

The availability of affordable medium- to long-term credit to sectors of the economy under served by commercial banks, but holding the potential for diversification, value addition and job creation for the low-skilled outside the enclave sector remains a challenge. Sectors of the economy that require long gestation periods and carry investment risks, such as agriculture, are not adequately served by the commercial banks. Drawing from lessons learned from the implementation of the Credit Stimulus Initiative launched in 2010, the Bank is considering modalities for providing medium-term resources for targeted lending. In this connection, the CBL recently launched the Loan Extension Assistance Facility (LEAF) for microfinance institutions, credit unions and village savings and loan associations under which L$200.0 million was made available for soft loans. The Bank has also decided to support the establishment of small rural finance institutions on a pilot basis in conjunction with interested commercial banks, including providing some of the seed capital as a loan for establishing such institutions. In addition, credit schemes for Liberian-owned SMEs and the agriculture sector are under consideration to become effective.

Enhancing Confidence in the Banking System

The reform of the banking system in the last few years has revived confidence in the banking system. The aim now is to consolidate that confidence, which will include, among others, stepping up efforts to deal with depositors' claims which linger as a legacy from failed banks many years ago. As a medium-term goal, the Bank will give due consideration to the establishment of a deposit insurance scheme.

Stepping Up the Ongoing Reform of the Foreign Exchange Bureaux

The CBL has made significant progress with the reform of the activities of foreign exchange bureaux, including the restructuring of the Association of Foreign Exchange Bureaux of Liberia (AFEBL), the strengthening of the financial capacity of licensed foreign exchange bureaux and improvement in their operational set up.

It should be noted that foreign exchange bureaux not registered or granted license by the CBL, after the deadline of January, 2012, are operating illegally. In this regard, the CBL will consider several enforcement actions in moving the reform process forward, including but not limited to shutting down and prosecuting illegal operators.

STEPPING UP EFFORT TOWARDS THE MODERNIZATION OF THE NATIONAL PAYMENTS SYSTEM

In 2011, the CBL made significant investment towards the construction of data centers for the payments system. Work is ongoing on the legal and regulatory framework to put in place an appropriate Payments System Law that states the powers of the Central Bank with respect to its oversight functions of the National Payments System.

The CBL believes that interoperability of the networks of financial institutions in the country is critical for efficiency in retail payments transaction. Commercial banks should, therefore, be guided by this position so that all interested parties are working together with the same objectives in mind.