BANK OF SIERRA LEONE

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ACRONYMS

ABSL	Apex Bank Sierra Leone Limited
ACH	Automated Clearing House
AFREXIMBANK	African Export and Import Bank
ATM	Automated Teller Machine
BN	Billion
BSD	Banking Supervision Department
BSL	Bank of Sierra Leone
CAR	Capital Adequacy Ratio
CBs	Commercial Banks
COMFIs	Credit-Only Microfinance Institutions
COVID	Corona Virus Disease
CRR	Cash Reserve Ratio
CPI	Consumer Price Index
CUs	Credit Unions
DHs	Discount Houses
DTMFIs	Deposit Taking Microfinance Institutions
EFT	Electronic Fund Transfer
EDMEs	Emergency Markets and Developing Economies
FEB	Foreign Exchange Bureaux
FMD	Financial Markets Department
FSA	Financial Services Associations
FSD	Financial Stability Department
FSR	Financial Stability Report
FX	Foreign Exchange
G2P	Government-to-People
GBP	Great Britain Pounds
GDP	Gross Domestic Products
GFSR	Global Financial Stability Report
GS	Government Securities
HHI	Herfindahl Hirschman Index
IFMIS	Integrated Financial Management Information System
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IMTOs	International Money Transfer Organizations
LCY	Local Currency
MAF	Ministry of Agriculture and Forestry
MFIs	Microfinance Institutions

MIX	Microfinance Information Exchange
MMOs	Mobile Money Operators
MPC	Monetary Policy Committee
MPR	Monetary Policy Rate
NASSIT	National Social Security and Insurance Trust
NBFI	Non-Bank Financial Intermediation
NLe	New Leone
NOP	Net Open Position
NPLs	Non-Performing Loans
NPS	National Payment Switch
OFISD	Other Financial Institutions Supervision Department
OMO	Open Market operations
O/N	Over Night
OSS	Operational Self Sufficiency
PAPSP	Pan African Payment and Settlement Platform
PAPSS	Pan African Payment and Settlement System
PaR	Portfolio at Risk
POS	Point of Sales
PSP	Payment Service Providers
PP	Percentage points
Q4	Quarter Four
ROA	Return on Assets
ROE	Return on Equity
RTGS	Real Time Gross Settlement System
SDF	Standing Deposit Facility
SLF	Standing Lending Facility
SLICOM	Sierra Leone Insurance Commission
TSA	Treasury Single Account
USD	United States Dollars
WAMZ	West African Monetary Zone
WEO	World Economic Outlook

GOVERNOR'S FOREWORD

I am delighted to present the seventh edition of the Financial Stability Report from the Bank of Sierra Leone (BSL). This report provides a comprehensive assessment of the financial system, with particular focus on the banking sector. The 2023 financial stability review holds significant importance due to the lingering effects of the COVID-19 pandemic, tight global financial conditions, the protracted Russia-Ukraine war, disruptions in global supply chains, and the escalating impacts of climate change. These factors have posed significant challenges to Sierra Leone and the global financial system, underscoring the necessity of a stable and resilient financial architecture to withstand such pressures.

Despite these challenges, Sierra Leone's financial system demonstrated resilience against both domestic and external shocks, achieving relatively robust performance in 2023. However, vulnerabilities persist in certain areas. While most financial soundness indicators monitored by the BSL exceeded prudential thresholds, issues such as high levels of Non-Performing Loans (NPLs), limited financial intermediation with concentrated credit exposure to a few sectors, and over-reliance on investments in government securities present systemic risks to the banking and financial system.

The BSL is well-prepared to address these challenges. Progress is being made in implementing the Basel II and Basel III frameworks while maintaining comprehensive regulatory and supervisory oversight. The Prudential Guidelines have been updated, and a risk-based supervisory approach has been adopted to enhance oversight. Additionally, numerous initiatives have been introduced to bolster public confidence in the financial system. These include the enactment of the Deposit Protection Fund Act, the issuing of the Financial Consumer Protection Guidelines, and the development of a Corporate Governance Framework for commercial banks. The Collateral Registry System has also been upgraded to enable the registration of both immovable and moveable assets. Individuals and non-incorporated entities can register security interests in accordance with the Borrowers and Lenders Act, 2019. Additionally, the National Payments Switch has significantly enhanced the payment infrastructure. The initial phase, which included ten institutions, was launched in May 2023. The second phase, now underway, shall introduce an Instant Payments Platform, connecting banks and mobile money operators through the National Payments Switch to facilitate instant payments between customers of different payment service providers.

In 2023, the banking sector's assets continued to grow, accounting for a significant proportion of the financial system's total assets relative to nominal GDP. However, the ratio of bank deposits and credit to GDP remained modest. However, the ongoing implementation of the National Strategy for Financial Inclusion (2022-2026), which in addition to prioritising the development of a stable, inclusive and accessible financial system with client-centric financial products and services, will also address the low levels of deposits and credit.

Looking ahead, the BSL remains committed to updating the financial regulatory framework to keep pace with domestic and global market dynamics. Policies will continue to be developed and implemented to address emerging challenges and to ensure financial system stability. It is my hope that stakeholders in the financial system will find this report informative and apply its insights effectively. More broadly, the BSL will remain dedicated to providing the public with direction and timely information on financial stability matters through the Financial Stability Report and the BSL's other communication channels.

Ibrahim L. Stevens, PhD
Governor, Bank of Sierra Leone

EXECUTIVE SUMMARY

Global Backdrop

The global economy faces high geopolitical tensions, economic fragmentation, and still tight financial conditions. In 2023, growth remained anemic, with weaker-than-expected performance in advanced economies and a property crisis in China affecting recovery. However, the latest IMF prediction is for world growth to accelerate to 3.2 percent in 2024 and 2025 respectively, due to resilience in the US, Emerging Markets and China.

In many emerging markets and developing economies (EMDEs), economic growth has not returned to pre-pandemic levels, and there are now larger disparities among regions. Advanced economies are expected to experience much slower growth in 2024 (1.8 percent) compared to the previous year (2.9 percent), due to waning momentum in the U.S, while growth in the Euro area is anticipated to increase slightly. Growth in EMDEs is forecast to remain broadly unchanged in 2024 (4.2 percent), as the growing momentum in India, South Africa, and Saudi Arabia is counterbalanced by slowing growth in China.

In 2023, global consumer price inflation declined (to 6.7 percent) due to slower economic growth, restrictive monetary conditions, and improvements in supply chains. It is projected to decrease further to 5.8 percent in 2024, bringing inflation back in line with most central banks' targets. Inflation in advanced economies is expected to decrease from 3.3 percent in 2023 to 2.6 percent in 2024.

The global banking sector has experienced a decline in acute stress, with the March 2023 banking scare confined to regional banks in the US and Credit Suisse. Rapid and substantial rate hikes in major advanced economies resulted in tight global monetary policy, with real rates above neutral rates expected to persist into 2025. Lending surveys in advanced economies suggest banks have restricted access to credit significantly over the past year, impacting real activity. Higher lending interest rates are likely to put banks under increasing pressure, while housing and commercial real estate markets have weakened. Bond market yields have also risen, though there is no immediate indication of a credit crunch.

The global banking system faces tension with weak banks still present. The Global Financial Stability Report (GFSR) recommends strong corporate governance and risk management, monitoring of asset classification, interest rate, and liquidity risks. Timely supervision, clear mandates, resources, and legal protection are essential. Countries should build buffers to support credit provision during stress periods. Reforms post-global financial crisis should include evaluating Basel III standards, expanding regulations, and addressing cross-border funding challenges. Non-bank financial intermediation is rising in importance, necessitating comprehensive systemic risk assessments. Climate financing in EMDEs requires various policies like carbon pricing, fiscal, structural, climate, and financial sector measures.

Economic Developments in Sierra Leone

Following the rebasing of real GDP figures, the economy has grown by 5.7 percent in 2023, with growth projected to slow to 4.0 percent in 2024. This deceleration is primarily attributed to weaker performance in the mining sector and declining international iron ore prices. In the medium term, however, the economy is expected to be on a recovery path, with GDP forecasted to grow by 4.5 percent in both 2025 and 2026, and further to 4.6 percent in 2027. This growth outlook reflects anticipated expansions in agricultural activities, a rebound in the mining sector, and sustained macroeconomic stability.

Nevertheless, potential risks remain, including higher commodity prices, trade disruptions due to developments in the Middle East and other geopolitical uncertainties, fiscal slippages, and spillover effects from ongoing global fragmentation, all of which pose challenges to the domestic economy going forward.

Inflation peaked at 54 percent in September 2023 but decreased to 52 percent by the end of the year. It further declined to 41 percent in March 2024, 32 percent in June 2024 and 25 percent in August 2024. Food and non-food prices dropped, contributing to the decline in headline inflation. The exchange rate stabilized since July 2023 and it continued to be relatively stable up to the second quarter of 2024, due to some policy measures by BSL like prohibiting offshore FX trading and strict monitoring of repatriation of export proceeds. Speculations in the FX market decreased in 2023 Q4, leading to reduced hedging activities by market participants.

Domestic Banking Sector

The banking sector continued to dominate the financial system, accounting for 85.0 percent of total assets. Despite slower growth, high inflation, and the rapid depreciation of the Leone amid the ongoing Russia-Ukraine conflict and geopolitical tensions, Sierra Leone's banking sector generally remained resilient. The sector as a whole was well-capitalised, profitable, and liquid. However, these positive financial indicators are largely attributable to the banking sector's significant exposure to the government, involving assets considered highly liquid and low risk. Government securities offered high nominal returns with a zero percent regulatory risk rating for capital. As a result, private sector credit remained very low by both international and regional standards, with further declines observed.

The banking sector saw an improvement in asset quality as Non-Performing Loans (NPLs) ratio decreased from 11.6 percent in 2022 to 8.8 percent in 2023, below the 10 percent regulatory threshold. Except for three banks, most banks had NPLs below the regulatory limit. The ratio of NPLs (net of provisions) to regulatory capital fell to 16.9 percent in 2023 from 21.7 percent in 2022. This trend is expected to continue as oversight of institutions with high NPLs improves.

At end December 2023, the CAR stood at 41.7 percent, with the Tier 1 CAR at 31.4 percent, significantly above the respective minimum regulatory requirements of 15.0 percent and 7.5 percent respectively. The banking sector remained very profitable. The Return on Equity (ROE) increased to 35.8 percent in 2023 from 26.0 percent in 2022 whilst the Return on Assets (ROA) increased to 7.9 percent from 5.5 percent in the previous year.

In 2023, the banking sector witnessed a large (over 40 percent) increase in pre-tax profit, outpacing cost growth with the cost-to-income ratio dropping significantly to 52 percent. Short-term investments in Government Securities were a major source of income, accounting for more than one-half (55.5 percent) of earnings.

The results of the Bank of Sierra Leone's stress tests indicate that the banking sector is generally resilient to adverse shocks that might arise in the future, even under conservative assumptions. Although extreme shocks could pose a systemic risk, the likelihood of this occurring is considered very low. None of the individual macro shock scenarios would cause the sector's capital adequacy ratio (CAR) to fall below 15.0 per cent. This resilience largely stems from banks' very high initial CAR levels, supported by substantial holdings of government securities, which are deemed risk-free and offer high returns. Consequently, even with severe shocks to credit risk, the sector's CAR remains above regulatory minimums.

Non-Bank Financial Sector

In December 2023, Other Financial Institutions (OFIs) remained stable with a constant number of DTMFIs, CBs, FSAs, MMOs, and DHs. However, the number of COMFIs increased to sixty-nine (69) and CUs decreased to twenty-five (25). DTMFIs expanded in terms of assets, equity, deposits, and loans, but their growth was lower than the inflation rate, resulting in a significant decline in real terms. The largest DTMFI accounted for 36.64 percent of the sector's assets.

The DTMFIs reported a much higher profit in 2023 as compared to 2022. Their Return on Assets (ROA) increased slightly but exceeded the minimum MIX standard of 2.1 percent. Their Return on Equity (ROE) however fell below the MIX benchmark of 13.6 percent.

As of December 2023, the total assets of reporting COMFIs increased to NLe633.81 million. Total loans also increased, mainly due to the rise in reporting COMFIs. Paid up capital grew by 24.2 percent, while total equity decreased by 15.1 percent. However, the profitability of COMFIs decreased in 2023. The consolidated OSS ratio was 101.8 percent, below the minimum MIX requirement of 112.00 percent. The consolidated ROA and ROE of COMFIs decreased significantly, primarily due to significant losses for ten (10) out of the thirty-nine (39) reporting COMFIs. Most of these institutions were new but are expected to gradually comply with regulatory requirements.

The assets of Community Banks increased in 2023, primarily due to increased investments and gross loans. The three largest CBs accounted for 39.3 percent of total assets, with investments increasing by 66.7 percent and gross loans by 15.3 percent. The profitability of the CB sector increased by 8.8 percent to NLe14.2 million, and net financial income increased by 12.9 percent to NLe35.3 million. Six (6) out of seventeen (17) CBs recorded profits, while the consolidated OSS was 134.3 percent, above the MIX Standard of 112 percent. However, six (6) out of seventeen (17) CBs did not meet the standard due to high NPLs. ROA decreased but still higher than the MIX standard of 2.1 percent.

The MMOs saw significant growth in activities, including the number of agents, accounts, and transaction value. In December 2023, the DHs sector reported a pre-tax profit of NLe0.6 million, slightly better than the previous year. The consolidated ROA and ROE were 1.6 percent and 4.5 percent, respectively. The cost-to-income ratio increased to 79.8 percent, but the Operational Self-Sufficiency ratio decreased to 125.3 percent. ABSL's financial performance was unsatisfactory, as it recorded a pre-tax loss of NLe2.4 million, worse than 2022's profit of NLe1.8 million.

In December 2023, the number of Credit Unions (CUs) decreased from twenty-seven (27) to twenty-five (25). Despite this, total membership increased by 12.2 percent to 16,494. The consolidated total assets of the CUs sector increased by NLe5.7 million to NLe30.0 million, while total savings increased to NLe19.6 million. Share capital and gross loans also increased by 43.6 percent and 14.7 percent, respectively.

The assets of the NASSIT pension scheme contracted by 6.7 percent during 2023. NASSIT, however, continues to generate sufficient funds to meet customers' needs. Although total income declined by 9.0 percent in 2023, contribution income still surpassed benefits payments by a wide margin, and remained sufficient to meet the fund's total expenses, giving rise to surplus for future investment or future use.

Financial Markets

The BSL raised its monetary policy rate (MPR) by 525 basis points from 17.0 percent in December 2022 to 22.25 percent in December 2023, while also increasing the overnight Standing Lending Facility (SLF) and Standing Deposit Facility rates to 25.25 percent and 15.75 percent respectively. In 2023, the Bank of Sierra Leone managed aggregate banking sector liquidity primarily through Open Market Operations (OMOs). Access to the Standing Lending Facility (SLF) window increased in the first half of the year but began to decline after July. The secondary market for Government Securities (GS) in Sierra Leone remained illiquid, as investors generally hold GS until maturity. Consequently, there is minimal security trading among commercial banks. The Bank of Sierra Leone is developing strategies to enhance liquidity in the secondary market for Government Securities. Commercial banks continued to dominate the primary market, which is heavily skewed towards 364-day tenures.

Payments System

The BSL monitors and evaluates the Financial Market Infrastructure to attain efficiency and safety, given its significance. It prioritizes financial inclusion, system protection, and stakeholder collaboration. Although non-cash transactions increased, cash transactions remained significant.

The National Payment System (NPS) is a World Bank-funded project aimed at improving retail payment infrastructures and rural connectivity. Phase one, which began in April 2023, involved six (6) banks and has grown to ten (10). The next phase will provide an Instant Payment Platform, connecting banks and mobile operators for instant payments between different providers.

Financial Stability Related Measures

The BSL is in charge of overseeing the banking sector’s supervision and regulation using a risk-based approach. It is now implementing migration to Basel II and Basel III capital regimes. Four banks - two of which are state-owned - remained under enhanced supervision, which is intended to improve their ability to withstand unanticipated shocks and to strengthen governance and credit administration. The two state-owned banks have, however, made good progress in terms of overall performance and profitability.

In order to improve the banking sector's credit quality, the BSL is currently developing a strategy for Non-Performing Loans (NPLs) which is expected to be published before the end of 2024. The Deposit Protection Act has been passed by Parliament and has been operationalized. The BSL is currently working on establishing the Deposit Protection Fund within the Bank's overall structure for establishing an efficient Framework for Crisis Management and Resolution following the passing of the Bill.

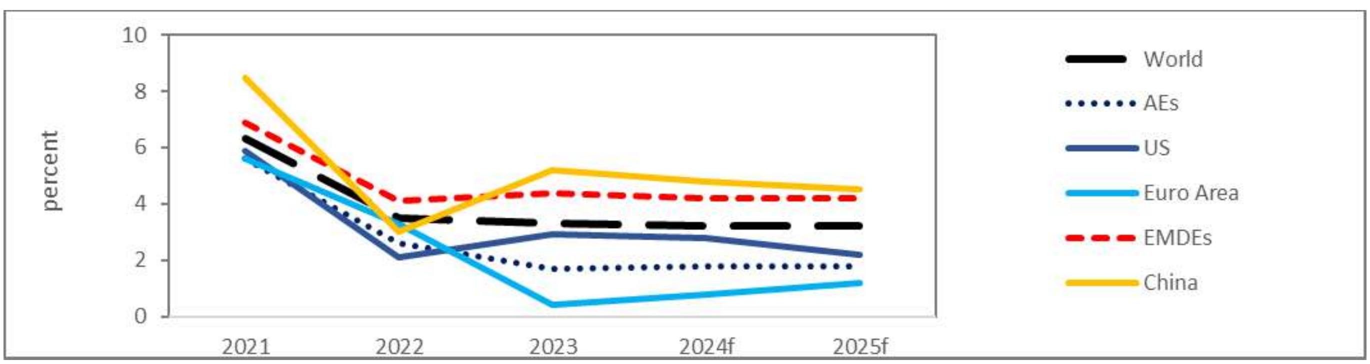
1 MACROECONOMIC AND FINANCIAL DEVELOPMENTS

1.1 Global Macroeconomic Developments

The global economy continued to be characterised by high geopolitical tensions, economic fragmentation, and tight financial conditions. Global growth remained weak in 2023, moderating to 3.0 percent from 3.4 percent in 2022. Slower-than-expected growth in advanced countries and the impact of the property crisis in China weighed on global recovery. The October 2024 IMF World Economic Outlook update (WEO) however projected global growth to accelerate to 3.2 percent in 2024 and 2025 respectively, because of greater-than-expected resilience in the United States and several large Emerging Markets and Developing Economies (EMDES), as well as fiscal support in China. While global headline inflation trended downwards, in many countries, including some major global economies, it remained higher than target. Commodity prices remained volatile amid climate-related and geopolitical shocks, representing a major risk to permanently reducing inflation. In most areas, inflation declined faster than anticipated due to tightening monetary policy and supply-side challenges that are gradually being resolved. The October 2024 IMF World Economic Outlook update (WEO) predicted global headline inflation to drop to 5.8 percent in 2024 and 4.3 percent in 2025.

Economic growth did not return to its pre-pandemic rate in many EMDEs, and there were widening deviations among regions. In advanced economies, growth is expected to remain slow at 1.8 percent in 2024, down from 1.7 percent in 2023, as US momentum fades while growth in the Euro area is expected to pick up. Growth in EMDEs is projected to remain unchanged in 2024 (at to 4.2 percent), as the increasing momentum in India, South-Africa and Saudi Arabia is offset by the slowing growth in China.

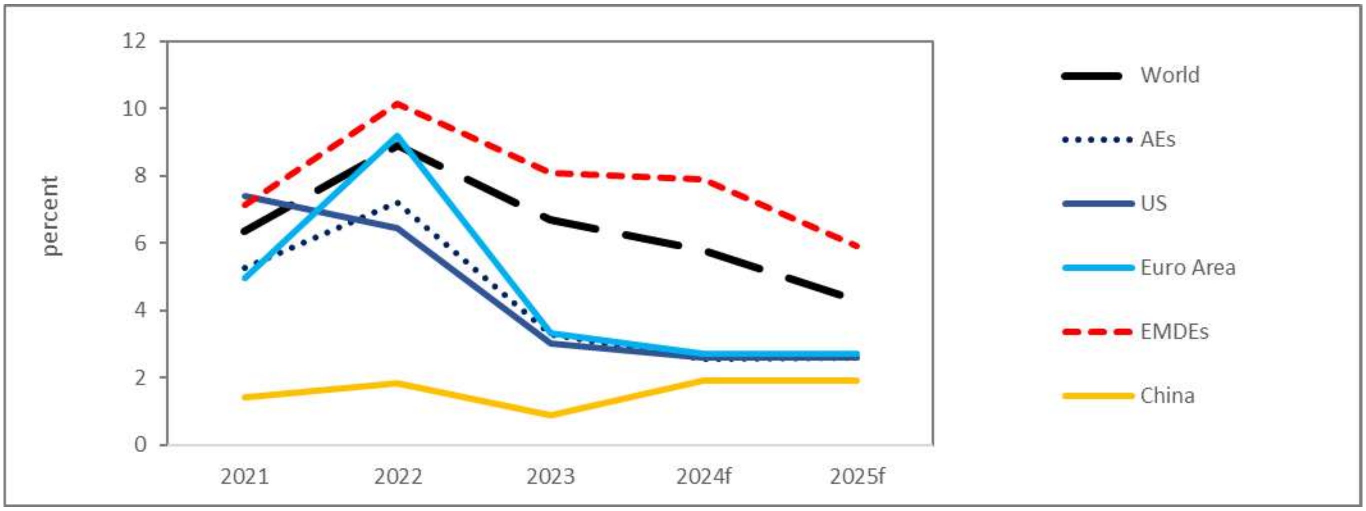
Figure 1.1: Annual Real GDP Growth (%)



S0urce: IMF, World Economic Outlook (WEO) October 2024 Update.

Global consumer price inflation declined in 2023, mainly as a result of slower economic growth, restrictive monetary conditions, and improvements in supply chains. Global inflation is projected to decelerate further in 2024 (to 5.8 percent) back closer in line with central bank targets. Inflation in advanced economies is expected to decrease from 3.3 percent in 2023 to 2.6 percent in 2024. The inflation rate in the U.S. is forecasted to reach 2.6 percent in 2024, which is closely aligned with the Federal Reserve's target of 2.0 percent. In the Eurozone, inflation remains above target throughout 2024. In EMDEs inflation is projected to decrease moderately from 8.1 percent in 2023 to 7.9 percent in 2024 and 5.9 percent in 2025. (*Figure* 1.2).

Figure 1.2: Developments in Global and Regional Annual Inflation



Source: IMF, World Economic Outlook (WEO) October 2024 Update.

1.2 Global Financial Developments

The global banking sector experienced moderate levels of stress, with the March 2023 banking scare limited to regional banks in the US and Credit Suisse. Large and rapid rate hikes in major advanced economies resulted in a tight monetary policy stance, with real rates above neutral rates expected to persist through to 2025. Lending surveys in the US and Europe suggest that banks have restricted access to credit significantly over the past year and are expected to continue doing so in the coming months.

Tighter credit conditions affected real activity in advanced economies, with credit and investment demand contracting in the first half of the year due to tighter supply and lower demand for credit. High interest rates are likely to put banks under increasing pressure in major economies, both directly and indirectly. Housing and commercial real estate markets have already been reacting, with house and commercial property prices slowing or reversing since the beginning of the tightening cycle in several countries. Bankruptcies remain lower than before the pandemic in most countries but are rising rapidly.

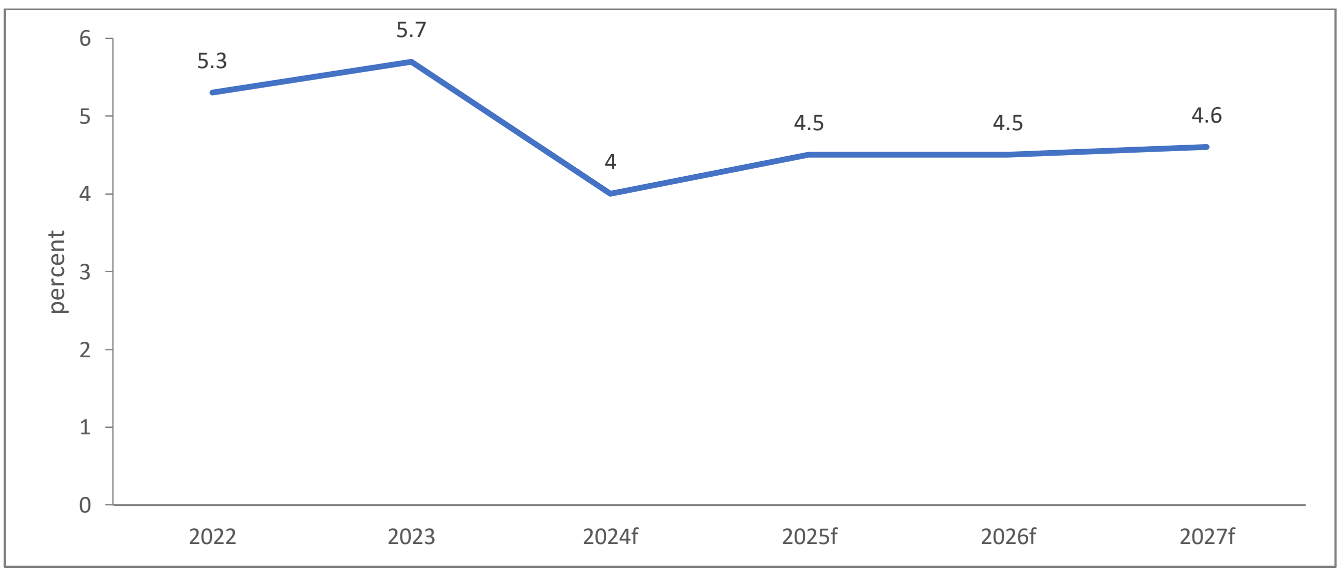
Yields in debt markets have started risen reflect the tighter monetary policy, while spreads to risk-free government debt have remained relatively constant. This suggests that although credit conditions have tightened significantly, there is no immediate indication of a credit crunch.

1.3 Domestic Macroeconomic Developments

1.3.1 GDP Growth and Inflation

The economy grew by 5.7 per cent in 2023, with growth expected to slow to 4.0 per cent in 2024. This deceleration is largely attributed to weaker performance in the mining sector, alongside declining international iron ore prices. In the medium term, the economy is expected to recover, with GDP projected to grow by 4.5 per cent in both 2025 and 2026 and further to 4.6 per cent in 2027. This outlook reflects anticipated expansion in agricultural activities, a rebound in the mining sector, and sustained macroeconomic stability. However, continuing risks, including higher commodity prices, trade flow disruptions associated with developments in the Middle East and other significant geopolitical uncertainties, fiscal slippages, and spillovers from ongoing global fragmentation, all pose challenges to the domestic economy going forward.

Figure 1.3: Real Annual GDP Growth in Sierra Leone



Source : Statistics Sierra Leone & IMF

Inflationary pressures rose during 2023, peaking at 54.59 percent in October but fell back to 52.16 percent in December. Both food and non-food inflation contributed to the drop in headline inflation, with nearly all the CPI basket's key components declining.

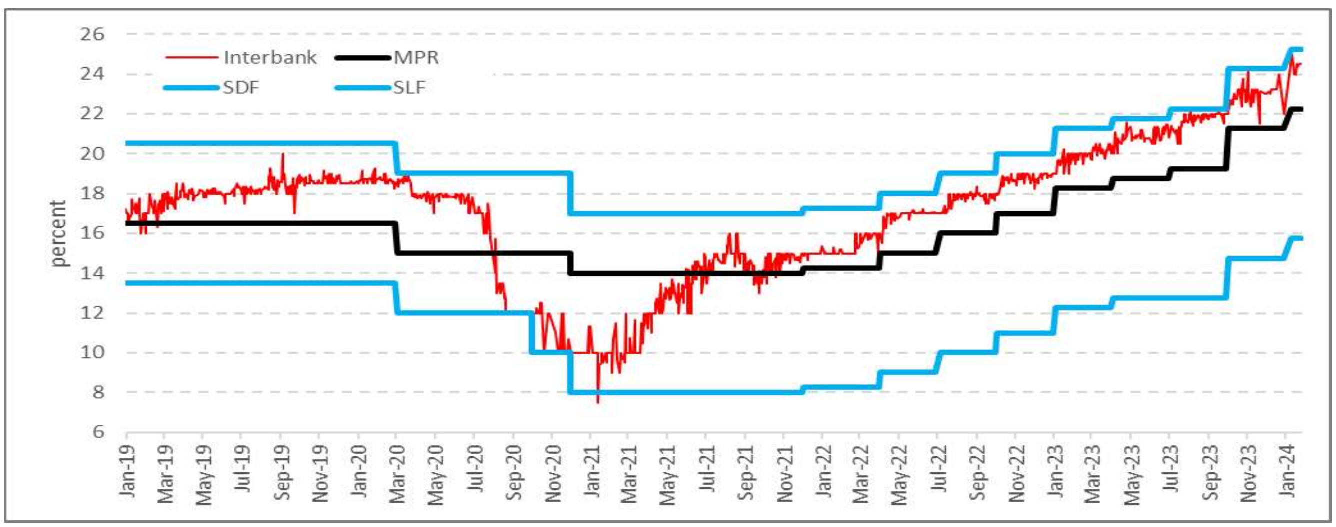
The exchange rate has remained relatively stable since July 2023, supported by policy measures implemented by the Bank of Sierra Leone, such as prohibiting offshore trading by international brokerage firms and enforcing the repatriation of export proceeds as outlined in the Finance Act 2024. Additionally, speculation in the FX market subsided in Q4 2023, resulting in reduced hedging activities by market participants.

1.4 Monetary Policy Management

Due to the persistent increase in inflation, the MPR was raised by a total of 4 percentage points (pp) in 2023. The rates for the standing lending facility (SLF) and the standing deposit facility (SDF) were adjusted by the same margin. The MPR was 22.25 percent, while the rate on the overnight standing lending facility (SLF) was 25.25 percent at the end of December 2023.

The interbank weighted average interest rate followed the changes in the policy rate, and on average it remained about 2pp higher than the MPR during 2023 indicating tight liquidity in the interbank market. This was reinforced by banks' persistent recourse to the overnight SLF. The reported average lending rate for commercial banks was 20.85 percent, with savings rate at 2.22 percent, while rates on time deposits for three months was 4.56 percent as of December 2023. As a result, the difference between commercial banks' average lending rate and savings rate was 18.63 percent in the same period. (*Figure* 1.4).

Figure 1.4: BSL Policy Rates and Interbank Weighted Average Rate

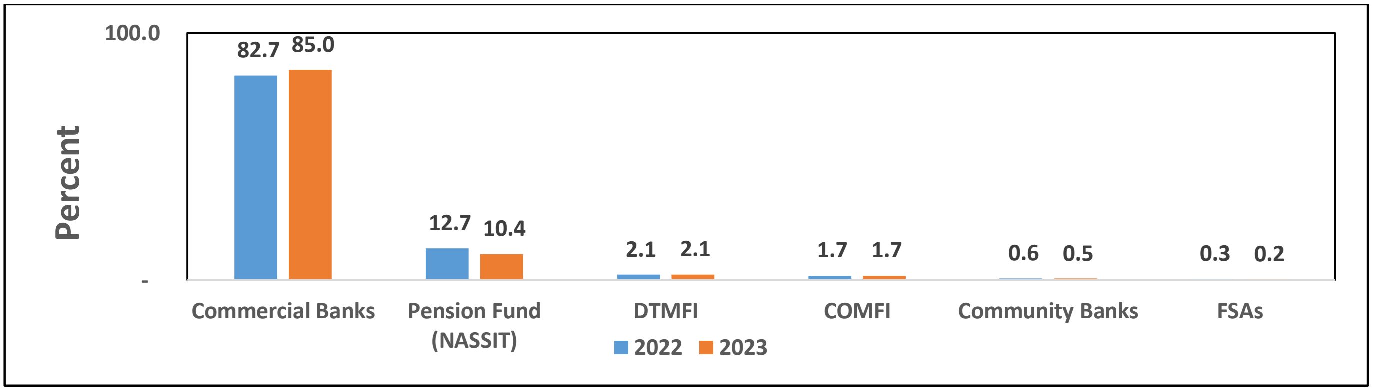


Note: MPR is the Monetary Policy Rate,
SDF and SLF is the overnight standing deposit facility and overnight standing lending facility rate, respectively.
The SDF rate is the lower while the SLF rate is the upper edge of the BSL's overnight interest rate corridor.
Source: FMD, BSL

1.5 Structure of the Financial System

The Banking sector further dominated the financial system accounting for 85.0 percent of the total assets in 2023, as compared to 82.5 percent in 2022 (*Figure* 1.5). It consists of fourteen commercial banks – two state-owned, two domestic privately-owned and ten foreign-owned, mainly Nigerian.

Figure 1.5: Share of Financial System Assets by Sector



Source: BSL and NASSIT

Pension funds ranked second with 10.4 percent of total financial system assets, though they declined by 2.3pp when compared to 2022. The other sectors of the financial system accounted for 4.6 percent of the total.

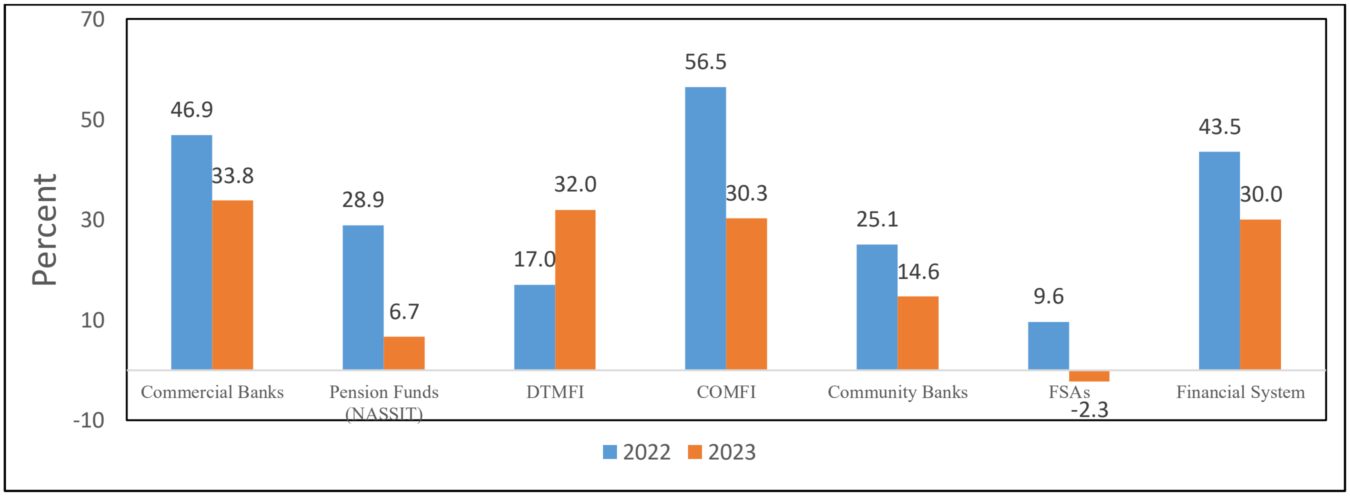
Box 1: Financial Institutions in Sierra Leone in 2023

The number of financial institutions in Sierra Leone increased in 2023. These include 14 commercial banks, 5 deposit-taking microfinance institutions (DTMFIs), 69 credit-only microfinance institutions (COMFIs), 17 community banks, 59 financial services associations (FSAs), 2 discount houses and 3 mobile money service providers. Also, the number of Foreign Exchange Bureaus increased from 80 as of December 2022 to 94 as of December 2023. The number of insurance companies regulated by SLICOM remained at 12 and there is one pension fund (NASSIT).

1.6 Total Assets of the Financial System

Total assets of the financial system grew by 30.0 percent in 2023. The growth was comprehensive with all sectors of the financial system contributing, even though the growth in the banking sector exceeded the growth in all the other sectors in the financial system. The FSAs sector however exhibited a negative growth in the same period. The banking sector registered asset growth of 33.8 percent. The growth in the banking sector however declined in nominal terms by almost one third when compared to the previous year's growth of 46.9 percent. The overall growth in the financial system declined by 13.5pp from 43.5 percent as of December 2022 to 30.0 percent as of December 2023 (*Figure* 1.6).

Figure 1.6: Growth of Assets in Sierra Leone's Financial System by Sector



Source: BSL and NASSIT

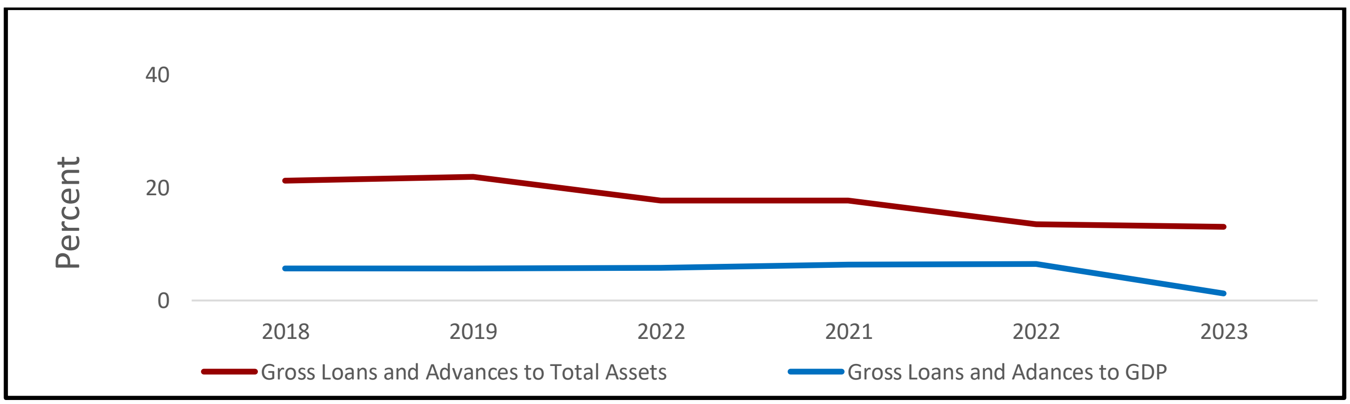
2 BANKING SECTOR ASSESSMENT

2.1 Summary

The banking sector in Sierra Leone exhibited resilience in the face of slowing domestic economic growth, high inflation, and rapid depreciation of the Leone in the wake of the still on-going Russia-Ukraine war and other geopolitical tensions. The sector continued to be well-capitalised, profitable, and liquid. However, the favourable financial indicators were largely due to the banking sector's significant exposure to the government and the associated assumed high liquidity and low risk of these investments. Government securities offered very high nominal returns, coupled with a zero percent regulatory risk rating. This was also reflected in an even lower ratio of credit to the private sector relative to GDP which is very low both by international and regional standards (Figure 2.1).

The sector embraced a hybrid service delivery model that combines in-person and remote services. The asset quality of the banking sector has improved recently due to the implementation of the loan write-off policy initiated by the Bank of Sierra Leone, better loan administration and recoveries and the superb risk-reward characteristics of government securities.

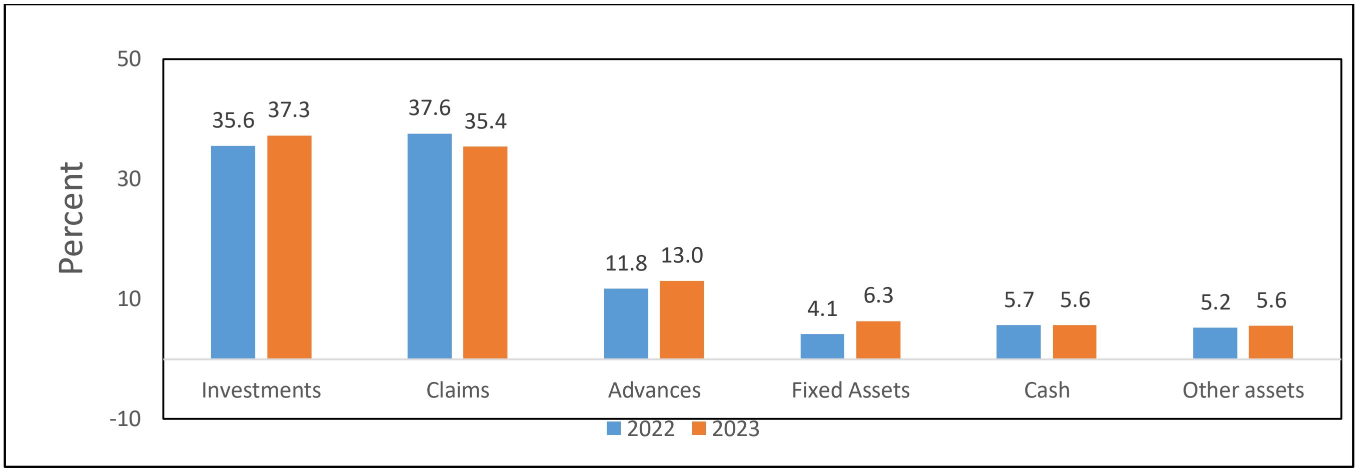
Figure 2.1: Gross Loans and Advances to GDP and Total Assets



Source: FSD, BSL

Investments had the largest share in the total assets of the banking sector, comprising 37.3 percent, followed by claims, which had a share of 35.4 percent. (*Figure 2.2*).

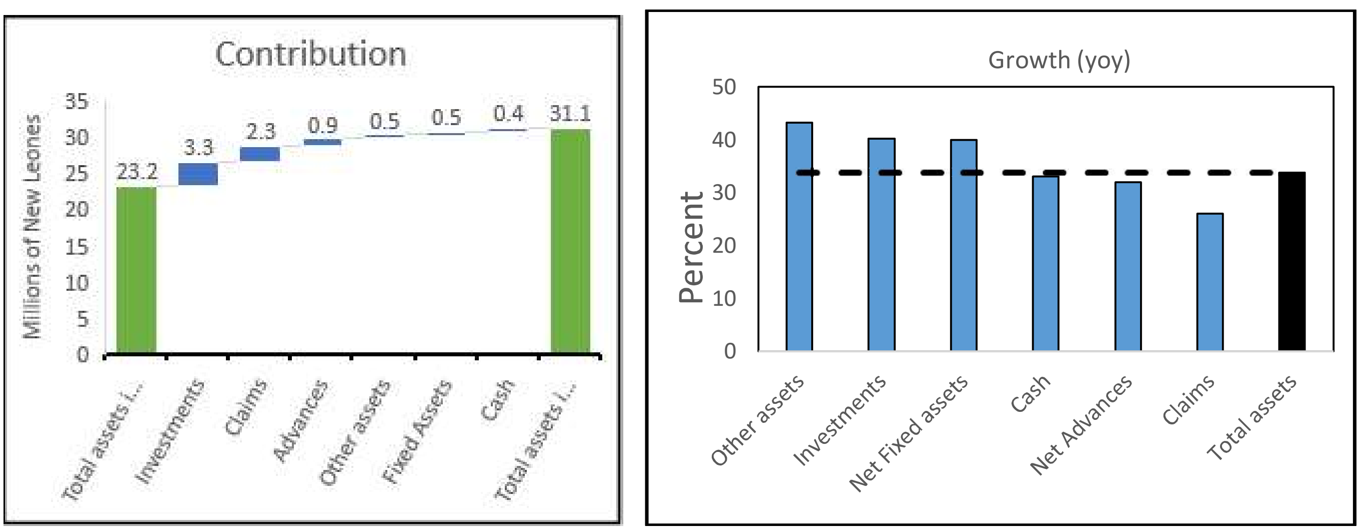
Figure 2.2: Share of Banking Sector Assets by Type



Source: FSD, BSL

Most asset classes registered a decline in real terms as their nominal growth stayed below the rate of inflation in the review period. Growth in assets was driven mainly by investments in government securities, and the growth rate in this activity was much higher than the growth of the banking sector's overall assets. Claims only increased by 26.0 percent, as the stabilizing exchange rate constrained the increase in the value of foreign currency placements. Fixed assets and other assets marginally increased by 2.2 percent and 0.4 percent respectively, whilst banks' vault cash marginally declined by 0.1 percent. (*Figure 2.2*).

Figure 2.3: Contribution to Growth and Growth Rate of Banking Sector Assets



Source: FSD, BSL

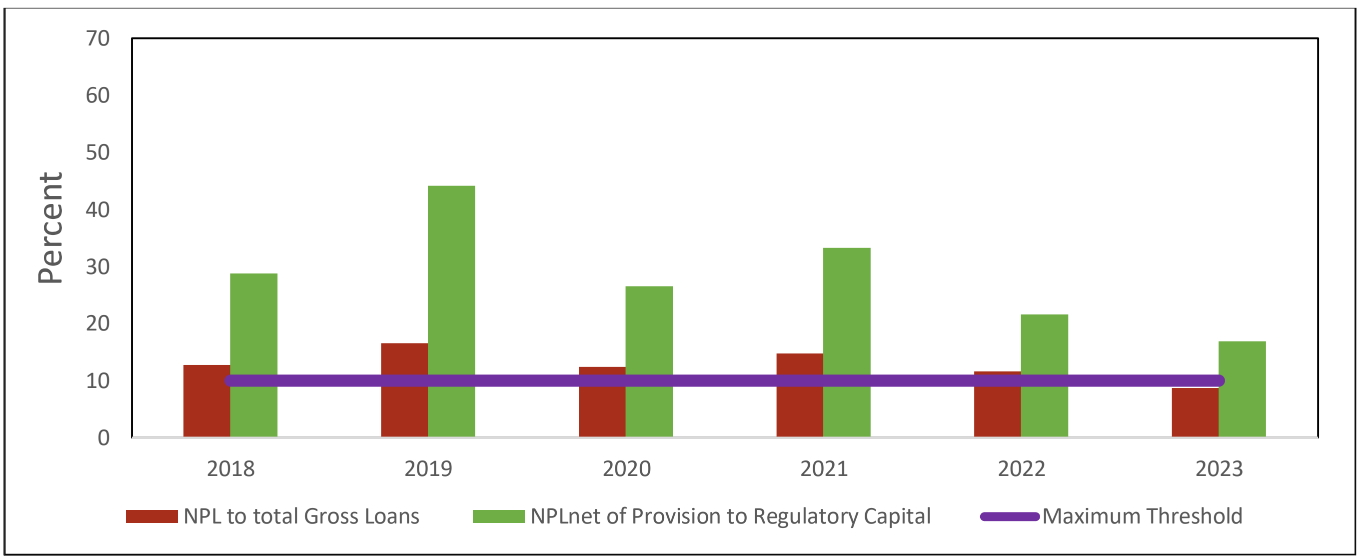
Claims were mainly driven by placement with foreign banks abroad. There were no other viable alternatives currently available for banks other than keeping foreign currency (cash) or placing these funds with foreign banks abroad or with the BSL to adequately manage their foreign exchange risk. Foreign currency cash in vault declined by 11.2 percent, while foreign currency placements with BSL abroad increased by 11.5 percent. As a result, after investment in government securities, foreign currency placements were the second-largest asset type on the balance sheet of the banking sector.

2.2 Credit Risk and Asset Quality

2.2.1 Non-Performing Loans (NPLs) and Provisioning

The ratio of banks' Non-Performing Loans to Total Gross Loans (NPLs) fell from 11.6 percent in 2022 to 8.8 percent in 2023 and to within the prudential threshold (10.0 percent). There was no significant variation in asset quality across banks since most of them, except for three banks, recorded NPLs below the regulatory limit. The NPL net of provisions to regulatory capital declined to 16.9 percent in 2023, from 21.7 percent recorded in 2022 (*Figure 2.4*). The banking sector's ability to both lend more money and absorb potential losses increased, as average asset quality continued to improve. The BSL anticipates that NPLs will continue to decline in the future on account of improved oversight of institutions with high NPL levels.

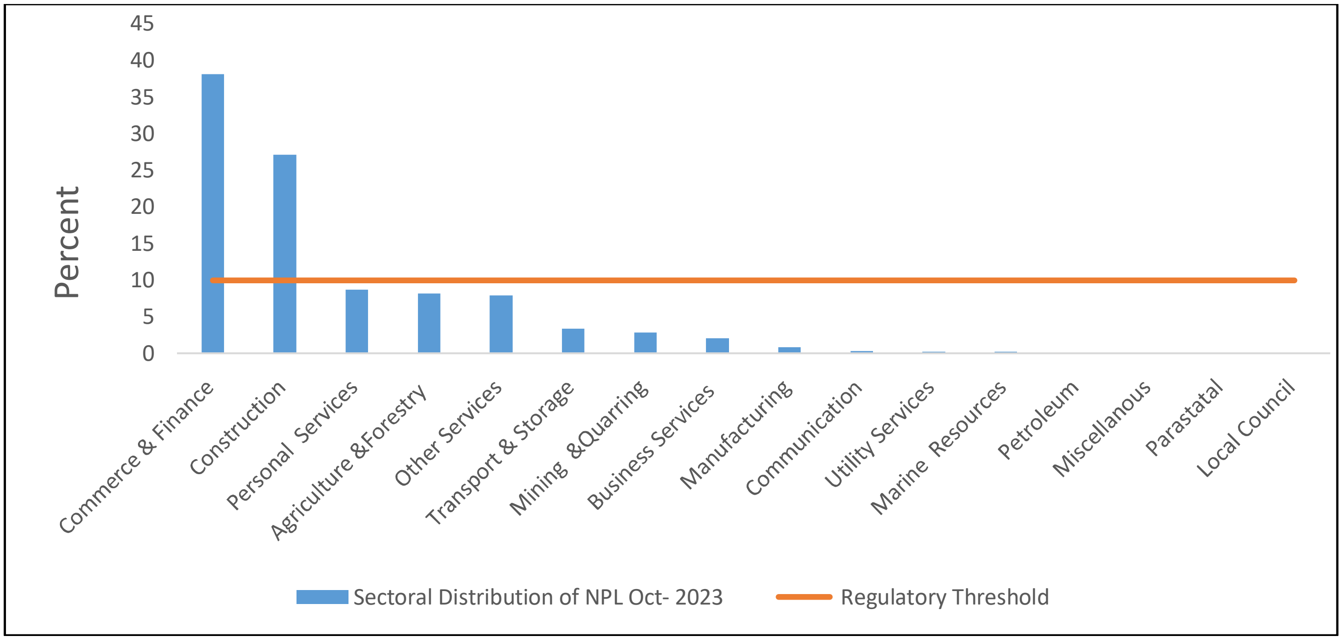
Figure 2.4: Asset Quality Indicators of the Banking Sector



Source: FSD, BSL

The two sectors with the largest contributions to total (NPLs) were the commerce & finance (38.1 percent) and the construction (27.1 percent) sectors. On the other hand, commerce and finance, personal services and business services sectors accounted for the largest portion of bank loans. These sectors (commerce and finance, business services) were also more vulnerable to supply chain disruptions and other global shocks. (*Figure 2.5*).

Figure 2.5: Sectoral Contribution to Banks' Total NPLs



Source: FSD, BSL

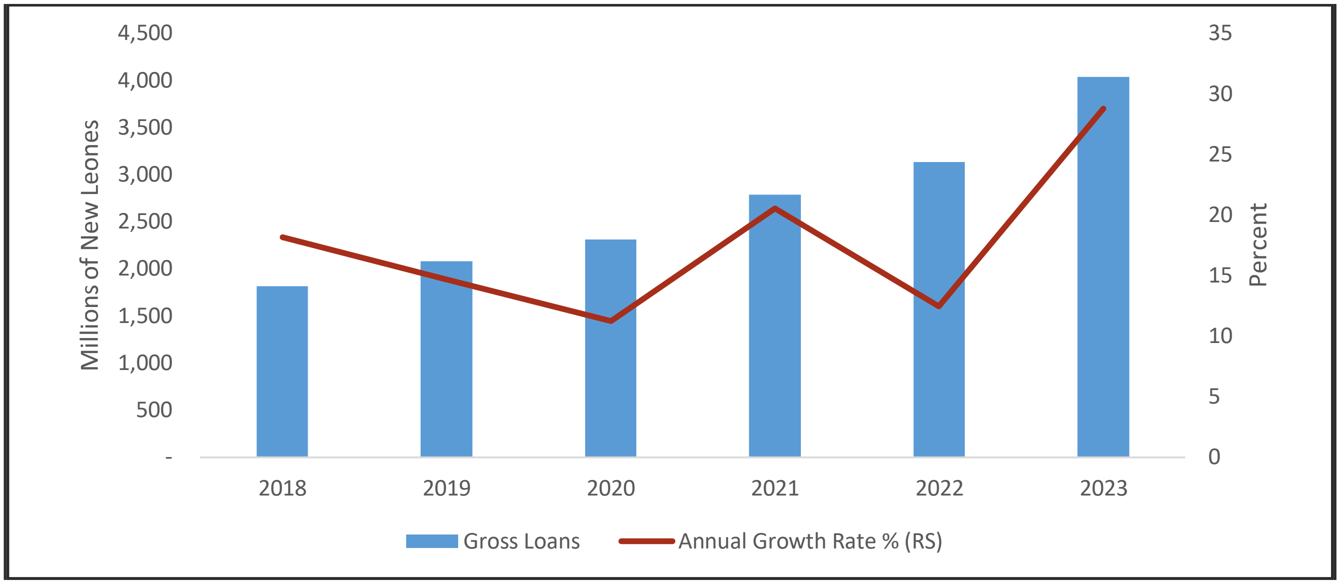
2.2.2 Credit Risk

In the year end-December 2023, gross loans and advances grew by 28.8 percent slightly less than total assets but significantly (?) less than the growth in prices and nominal GDP. The decline of loans and advances in real terms could reflect banks' restricted commercial prospects and/or customers' reluctance to take out loans due to the large rise in nominal interest rates. The primary cause appears to come from the loan supply side. There are, or at least perceived to be, a dearth of projects in Sierra Leone that have suitable risk-return characteristics that banks would be prepared to fund, especially in the presence of the very attractive alternative of investing in government securities.

The banks' loan-to-domestic deposit ratio rose slightly in 2023, to 39 percent, but remained well below the regulatory ceiling of 80 percent. Most of the increase in deposits was invested instead in Government Securities (GSs).

Overall, given the low level of loan penetration, the banks' exposure to credit risk was very low.

Figure 2.6: Level and Growth of Gross Loans and Advances



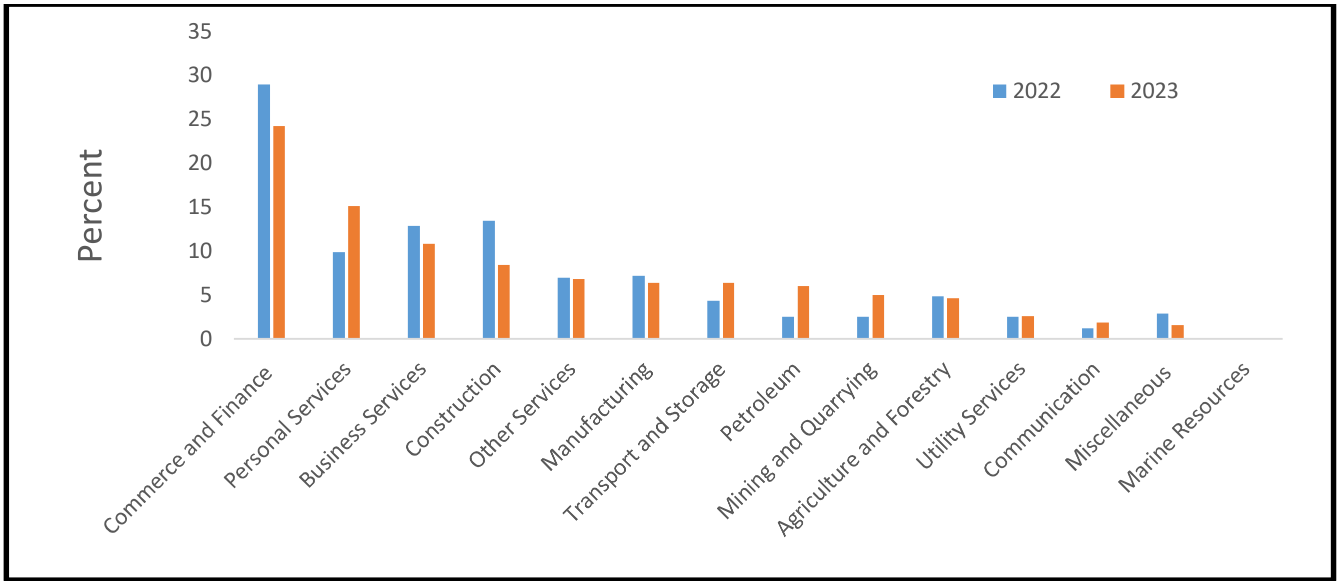
Source: FSD, BSL

2.2.3 Credit Risk from Sectoral Shocks

At end 2023, banks loans continued to be concentrated in the commerce & finance, personal services and business services sectors although less in the construction sector than in the previous year (Figure 2.7).

Sierra Leone is largely dependent on imports for most of its necessities, and the commerce & finance, manufacturing and mining sectors are major components in the country's import and distribution category. Banks' credit risks to these sectors, therefore, are sensitive to the global external environment especially disruptions in global supply chains, resulting from the continuing conflict between Russia and Ukraine and that in the Middle East and shocks to the Leone exchange rate.

Figure 2.7: Sectoral Distribution of Gross Loans



Source: FSD, BSL

2.2.4 Large Exposure Risk

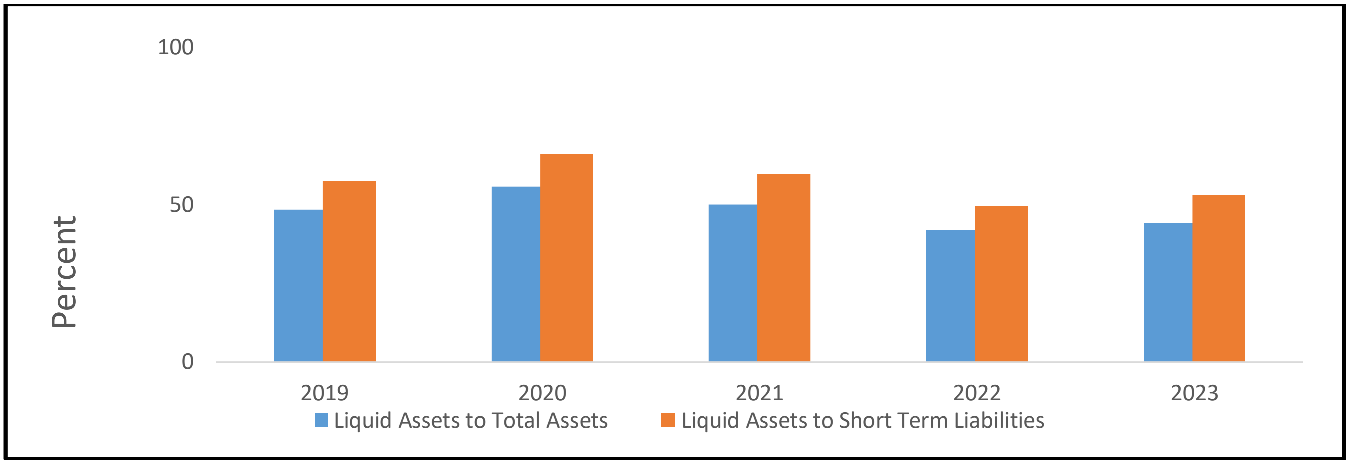
The industry's 50 largest credit exposures accounted for 83 percent of the banking sector's aggregate exposures and 102 percent of its capital base at end-December 2023. The largest single borrower alone accounted for 13 percent of aggregate exposures and almost 16 percent of the capital base. Therefore, banks' loans remain highly concentrated to just a few high value customers.

2.3 Liquidity Risk

2.3.1 Liquidity Assets

The banking sector remained well equipped to meet its short and long-term liquidity commitments. The ratio of liquid assets to total assets (44 percent) and to short-term liabilities (53 percent) increased even further in 2023 (*Figure 2.8*).

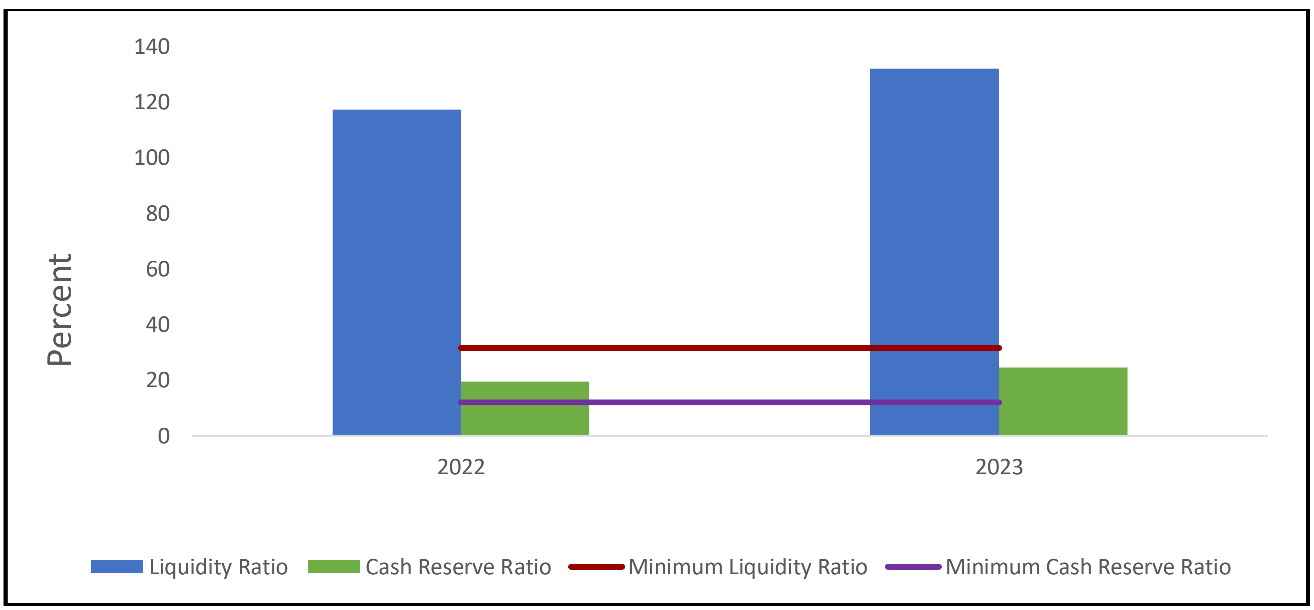
Figure 2.8: Liquidity Indicators of the Banking System



Source: FSD, BSL

The liquidity ratio and the cash reserve ratio (CRR) also rose further and are both well above their respective minimum thresholds (*Figure 2.9*). This resulted from the banking sector's substantial holdings of Government Securities (GS), which are considered as liquid. Although there is no well-functioning, deep and liquid secondary Government Securities market, the liquidity of GS derives from their eligibility as collateral for the BSL's SLF and the general understanding that GS can always be sold to the BSL if necessary.

Figure 2.9: Banking System Liquidity Performance against the Minimum Requirements



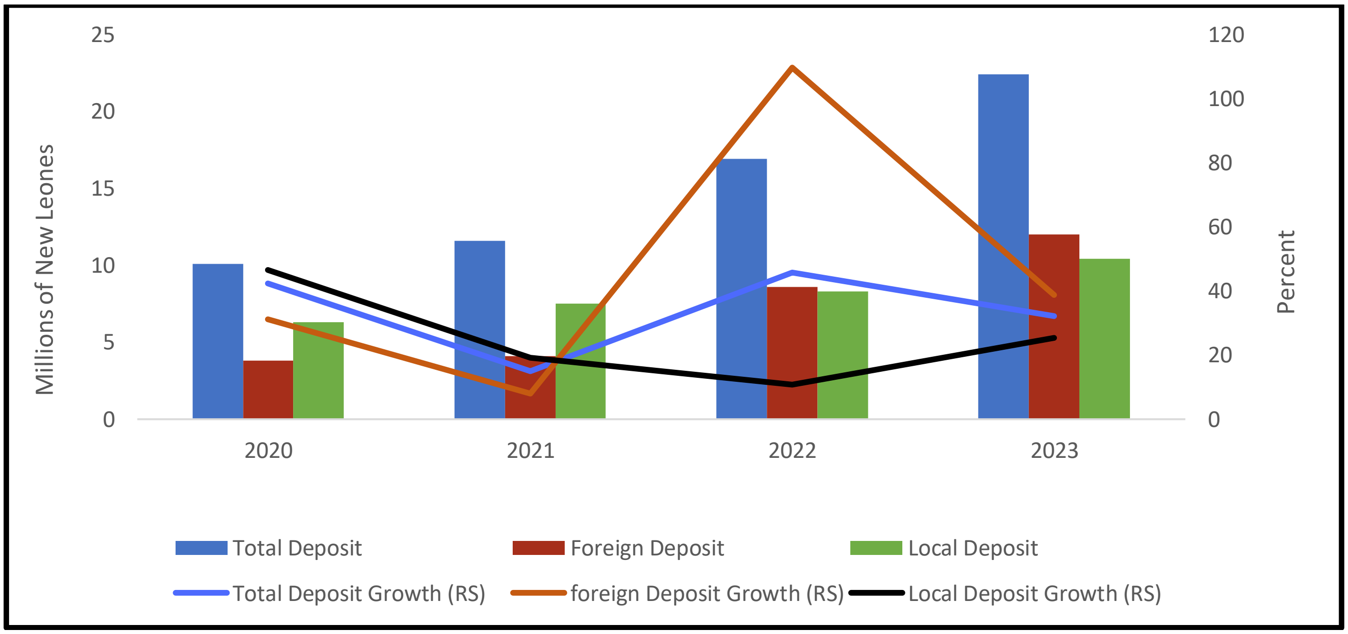
Source: FSD, BSL

2.3.2 Sources of Funding

Deposits continued to be the primary source of funding for the banking industry. In 2023, total deposits in the banking sector grew by 32 percent, but significantly slower than in 2022 (46 per cent). This was partially due to the exchange rate movement as the sharp decline in the value of the local currency led to large increase in the local currency value of foreign currency deposits in 2023, while the relative stability of the exchange rate towards the end of 2023 restrained their growth.

Because foreign exchange (FX) assets were perceived as superior stores of value, customers' desire to keep FX deposits surged due to the sharp decline in the value of the Leone relative to major international currencies. The average interest rates on local currency savings deposits were 2.2 percent, the return on government securities notably the one-year Treasury Bills remained at 36 percent in December 2023, while the Leone depreciated by about 22 percent. Thus, local savings mechanisms were unable to match the unchecked inflation that rose gradually until October 2023, when it peaked at 54.2 percent and then took a slow downwards movement to end at 52.6 in December 2023.

Figure 2.10: Composition of Banking Sector Deposits



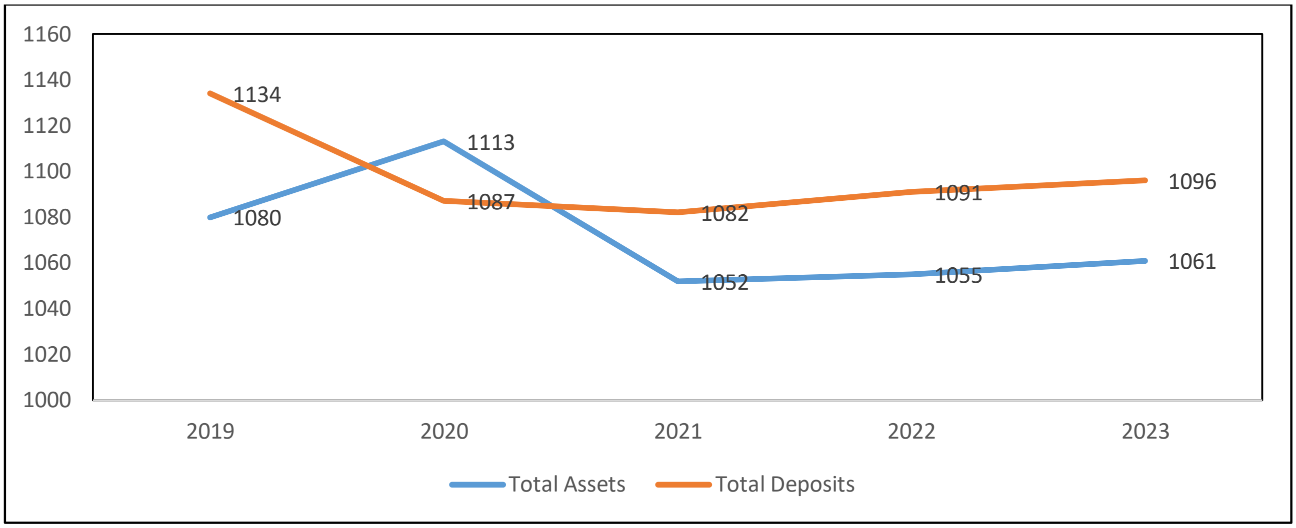
Source: FSD, BSL

Deposit concentration declined slightly in 2023, with the top 20 depositors accounting for 28 percent of the sector's total deposits. The single largest depositor held 8 percent of all deposits. However, banks remain exposed to significant liquidity risk in the event of unexpected withdrawals from the largest depositors. Furthermore, currency substitution may have contributed towards the reduction in deposit concentration, as a greater proportion of the population with normally lower levels of savings may have begun to transfer their assets to FX.

2.3.3 Risk of Contagion

The banking sector remains concentrated with the five largest banks share of both total deposits and total assets at 82 per cent. According to the more comprehensive Herfindahl-Hirschman Index (HHI) total asset and deposit concentration in the banking sector rose somewhat in 2023 but remained well below 1,500 – suggesting it is a competitive market *(Figure 2.11*).

Figure 2.11: Herfindahl-Hirschman Index



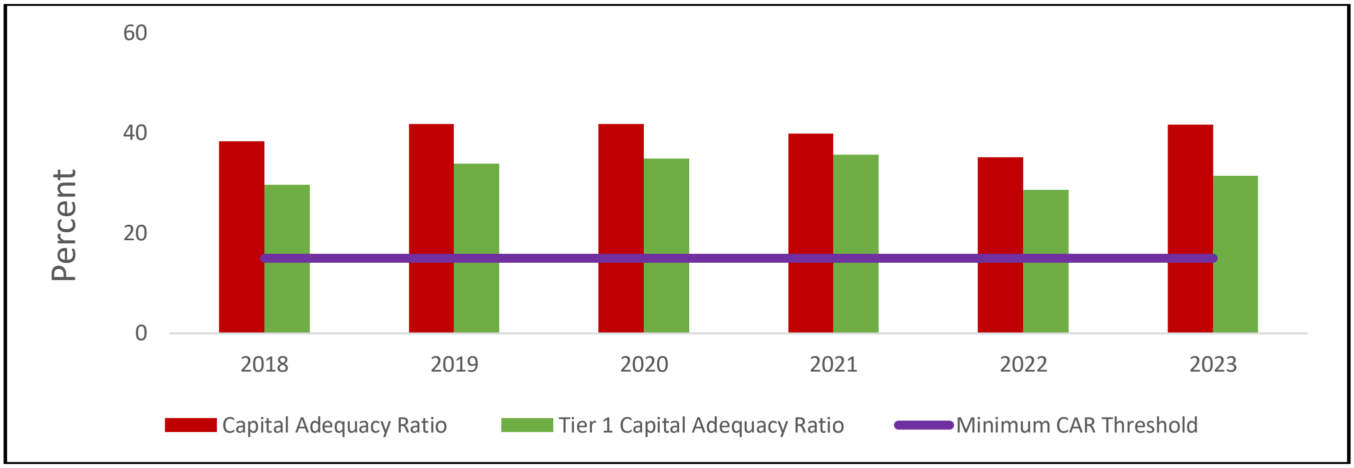
Note: Theoretically, a HHI of less than 1500 is considered a competitive market. The HHI values for bank assets and deposits were 1061 and 1096 respectively, indicating that the banking sector in Sierra Leone is competitive.
Source: FSD, BSL

2.4 Resilience

2.4.1 Capital Adequacy Ratio

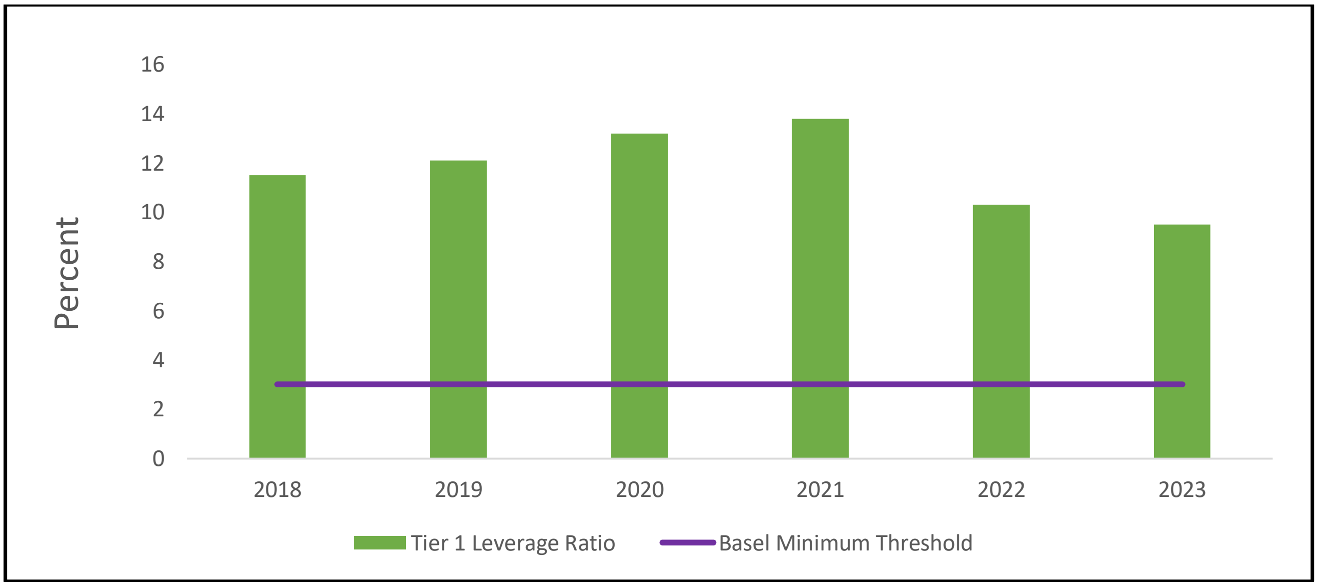
The Capital Adequacy Ratio (CAR) for the banking sector as a whole remained much higher than the BSL regulatory minimum. At end 2023, the CAR was 41.7 percent, while the Tier 1 CAR was 31.4 percent. These figures were much higher than the respective minimal regulation requirements of 15.0 percent and 7.5 percent respectively. Both CAR and Tier 1 CAR grew in comparison to 2022, mostly due to the high profitability of the banks.

Figure 2.11: Capital Adequacy Ratios of the Banking Sector



Source: FSD, BSL

Figure 2.12: Banking Sector Tier 1 Leverage Ratio



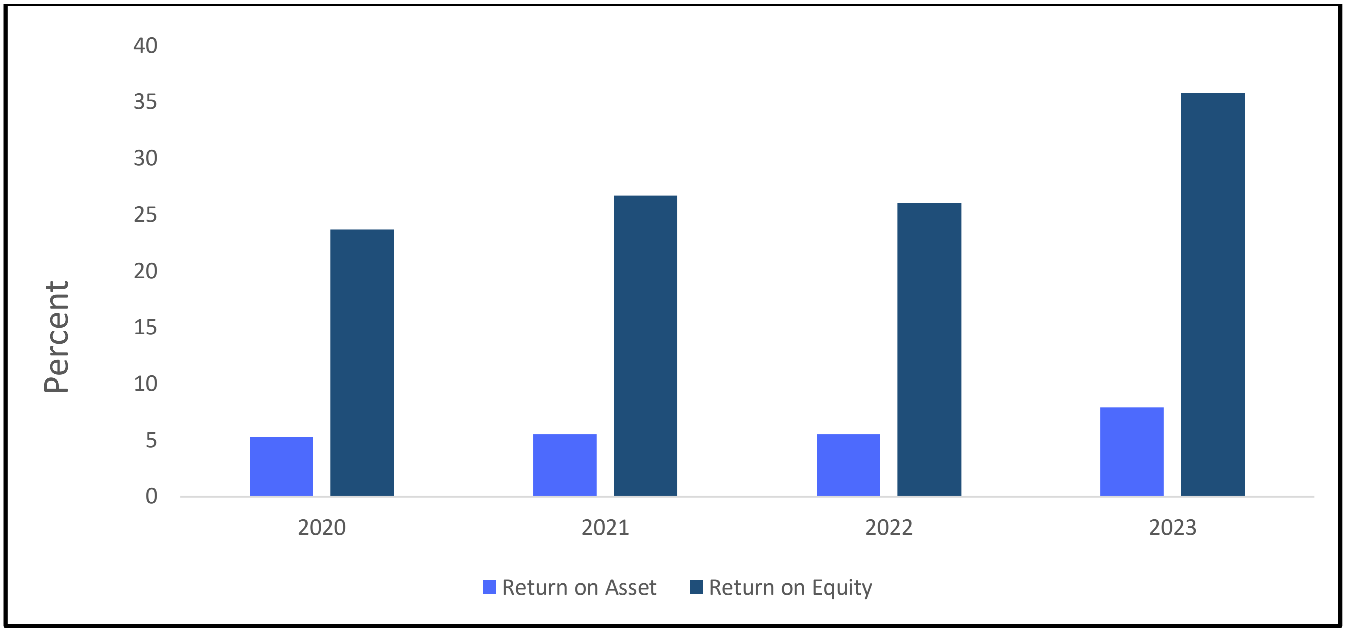
Source: FSD, BSL

The Tier 1 Leverage Ratio shows the amount of (Tier 1) capital relative to (unweighted) total assets. This ratio remained above the Basel III minimum level of 3.0 percent, indicating a well-capitalized and healthy banking sector. It, however, decreased slightly to 9.5 percent in 2023, from 10.3 percent in 2022.

2.4.2 Profitability

The banking sector remained very profitable with further increases in the Return on Assets and the Return on Equity (*Figure 2.13*).

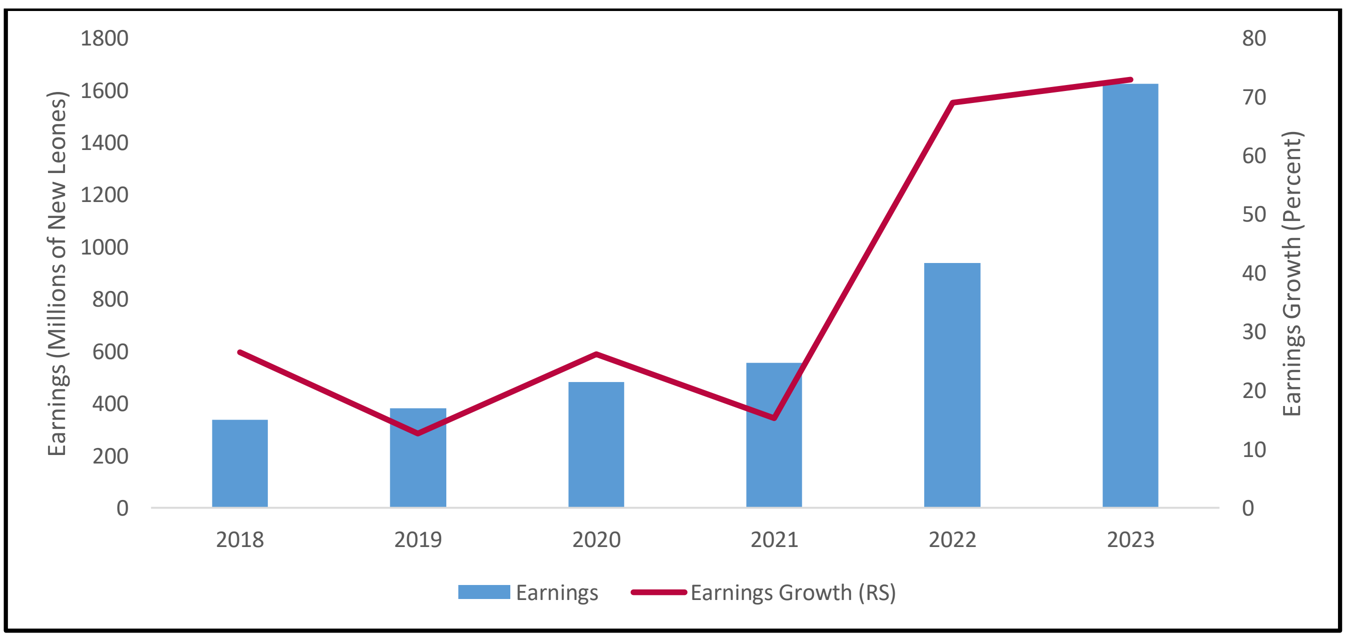
Figure 2.13: Profitability Indicators of the Banking Sector



Source: FSD, BSL

The growth in banks' earnings increased at a significantly faster rate (71 percent) than costs. Consequently, in 2023, the banking sector's cost-to-income ratio fell (to 52 percent). The return on short-term investments in government securities accounted for more than one-half (55.5 percent) of earnings.

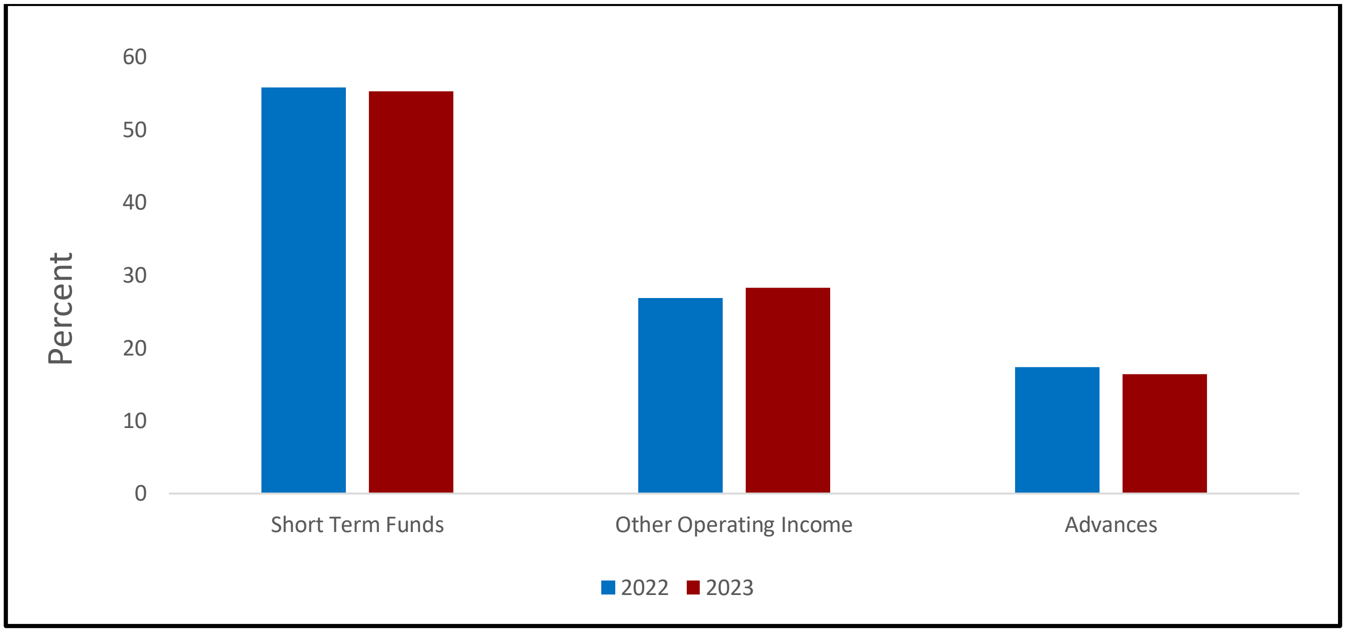
Figure 2.14: Earnings and Earnings Growth, 2018-2023



Source: FSD, BSL

The longer-term business viability of the banking sector faces challenges given the heavy reliance on revenue from Government Securities. Eventually, the nominal interest rate on GSs will likely decline as the government strengthens its fiscal position and inflation returns to target, which will probably also implify a slower increase in the supply of GSs. A risk of financial repression that lowers yields on government assets also exists, based on historical data. Regardless of these reasons, a large drop in yields on Government Securities poses a huge risk to banks' profitability and liquidity, and if sustained over a longer period, even to their capital adequacy.

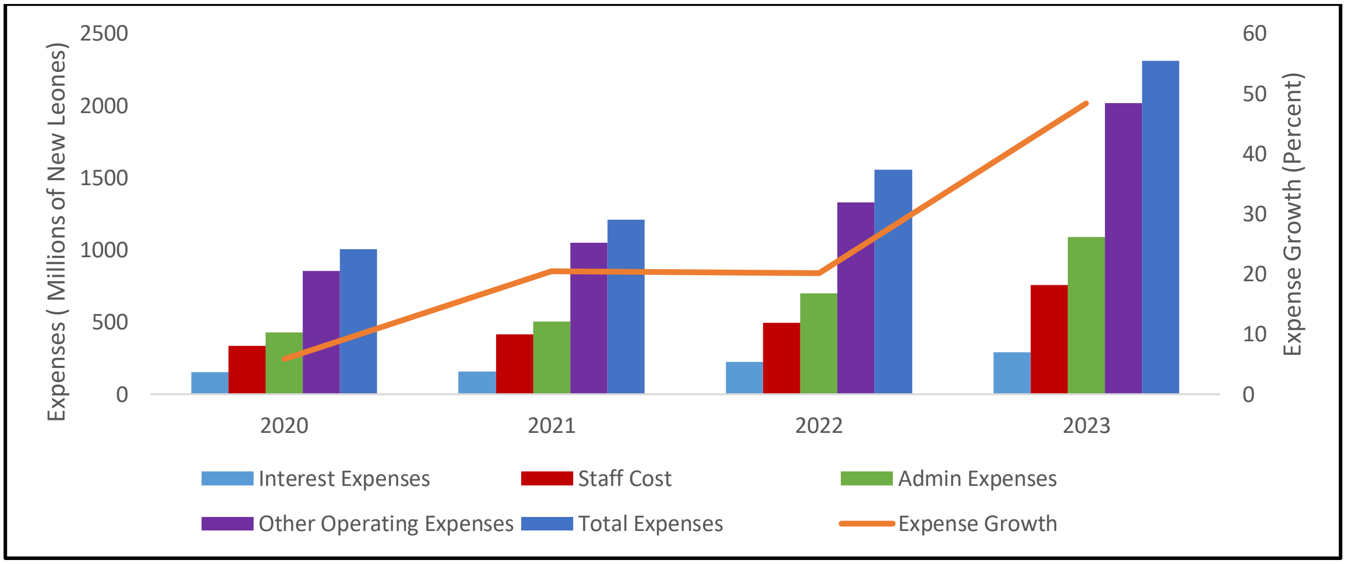
Figure 2.15: Composition of Banking Sector Income



Source: FSD, BSL

In 2023, expenses in the banking sector increased by 48.4 percent. The primary drivers of this expansion remained personnel and administrative costs. Staff expenses increased by 53.1 percent, while administrative costs also increased by 55.7 percent. Administrative costs increased in line with the rate of inflation.

Figure 2.16: Breakdown and Growth of Total Expenses



Source: FSD, BSL

2.5 Sources of Key Risks and Vulnerabilities

2.5.1 Non-performing Loans (NPLs) and Concentration Risks

In 2023, although the overall Capital Adequacy Ratio (CRR) seems robust and comfortably within tolerable limits, and NPLs for the sector as a whole fell below the prudential ceiling (to below 9 percent) there were still concerns regarding the quality of the assets. A few banks still had extremely high NPLs, which ranged between 15 percent and 20 percent.

Given that the 50 biggest bank borrowers represented 83 percent of aggregate exposures in 2023, there was a substantial danger of credit concentration in the banking sector. There were differences among banks, with some above the single obligor limit of 25.0 percent on largest borrower's exposure to capital base, even though it stood at 15.7 percent for the entire sector.

Bank deposits were also highly concentrated, with the top 20 customers accounting for 28 percent of all deposits, while the largest single depositor accounted for 8 percent of the total.

2.5.2 Viability of business models over the medium-term

Banks loan books were small in relation to their total assets, and bank intermediation was very low in relation to GDP. Net loans to the banking sector made up just 11.6 percent of total assets. The net loans to total assets ratio ranged from 2.8 percent to 25.0 percent for the individual banks in the sector.

Banks were not lending significantly to the private sector partly because of the crowding out effect of investment in government securities and lending was concentrated in a few customers or sectors of the economy.

Over half of all outstanding loans were accounted for by business and financial services, personal services, and commerce. Credit was still heavily concentrated in a small number of economic sectors.

As discussed above, the banking sector's profits were largely dependent on its investments in Government Securities, which offered a large spread, using mainly customers' deposits for this purpose. About 36 percent of the banks' assets consisted of government securities alone. Lower net interest revenue for the banking sector could have a substantial negative impact on profitability, should the government lower the rate of interest it pays on these instruments.

2.5.3 Currency substitution

In 2023, the proportion of total deposits denominated in foreign currency (FX) rose to 54 percent, with most of these funds held in foreign banks. Consequently, the banking sector became more susceptible to liquidity and market risk due to the significant share of FX-denominated liabilities and assets. This vulnerability was particularly pronounced for banks with short net open positions (NOP), as managing these positions grew increasingly challenging. For the sector as a whole, the single currency NOP to capital base stood at 0.4 per cent, and the aggregate NOP was 14.1 per cent, both within the regulatory limits of ±15 per cent and ±25 per cent, respectively. Of the fourteen banks, eight held short FX positions, while six had long positions. However, four banks breached their NOP limits, with some exceeding these limits by a considerable margin.

2.6 Non-Compliance Issues

The banking sector continued to be adequately capitalized. However, one of the banks recorded a CAR below the minimum 15.0 percent ratio and it had a negative position throughout the review period. The bank has however been placed under enhanced supervision and requested to develop a capital restoration plan.

2.7 Banking Sector Regulatory and Supervisory Developments

The BSL is responsible for overseeing banking sector supervision and regulation using a risk-based approach. The Bank is now pursuing the implementation and migration of the Basel II and Basel III capital regimes. Four banks—two of which are state-owned—remained under enhanced supervision, which is intended to improve their ability to withstand unanticipated shocks and to strengthen governance and credit administration. The two state-owned banks have however made great progress in terms of overall performance and profitability.

To boost the banking sector's credit performance, the BSL is currently developing an NPL Strategy which is expected to be published before the end of 2024.

The Deposit Protection Act has been passed by Parliament and has been operationalized. The BSL is currently working on establishing the Deposit Protection Fund within the Bank's overall structure for establishing an efficient framework for Crisis Management and Resolution following the passing of the Bill.

2.8 Conclusion

The banking sector remained robust, stable, and well capitalised. The sector’s regulatory capital ratio increased during the year, with profitability and liquidity ratios remaining very high. This was mostly due to the banking sector's substantial holdings of Government Securities (GS), which offered high returns, carried zero regulatory risk weights, and were deemed liquid. However, in the medium-term, the existing business model of the banks, which favors heavy investments in Government Securities rather than providing loans to the private sector is likely unsustainable. It is also undesirable since greater private credit deepening and widening can help support faster economic growth and increase financial inclusion.

With one exception, all banks met the new minimum paid up capital requirement. The Tier 1 leverage ratio marginally fell but remained well above the minimum regulatory threshold.

The decline and volatility of the Leone, the increase in currency substitution, and the challenges banks face in managing their foreign exchange net open positions were all contributing factors to the rise in exchange rate risks. Because of the pressure on open positions caused by the continual increase in FX deposits, it could result in difficulties in making additional investments in local currency Government Securities because of currency substitution effect.

3 SYSTEMIC RISKS ASSESSMENT

3.1 Stress Tests of the Banking Sector

The BSL conducted its regular stress tests to assess the banking sector's resilience to potential future shocks. These tests involved evaluating the impact of severe but plausible scenarios on banks' balance sheets and profit and loss accounts based on end-2023 data. The goal was to identify risks and vulnerabilities in the sector and assess the sector's ability to withstand adverse conditions. The tests evaluated credit, liquidity, interest rate and foreign currency risks on the fourteen banks. The stability of the banking sector is crucial for overall financial stability, as it controls a significant portion of total financial sector assets. Other non-bank financial sectors were either interconnected with banks or pose minimal threats due to their smaller size.

Five scenarios, including a baseline and scenarios with increasing degree of severity involving reduced government appetite for domestic borrowing, recession, liquidity issues, and a combination of factors, were simulated to test banks' capital buffers. The scenarios were based on potential future shocks, but their construction was guided by past events.

Credit risk stress tests involve three shock scenarios: proportional increase in NPLs, sectoral shocks to NPLs, and shocks to large exposures. Interest rate stress tests focused on changes in Treasury bill yields due to banks' heavy investment in government securities. Liquidity risk is assessed to measure the impact on banks' ability to meet short-term obligations during a liquidity squeeze.

3.2 Risk Scenarios for Stress Testing

3.2.1 Baseline

The baseline scenario is dependent on the current forecasts and expectations of the BSL. In the baseline, GDP is expected to grow by 4.7 percent in 2024 and 5.2 percent in 2025. Annual inflation is forecast to decline to 25 percent by end 2024 and 12.25 percent by end December 2025. The Leone is assumed to remain stable.

3.2.2 Interest rate risk: reduced local currency borrowing of the government.

This scenario presupposes a significant reduction in nominal interest rates, particularly in T-bill yields, which would lower the banks' interest revenue and profit. Given that commercial banks mostly invest in

364-day T-bills because of their relatively high yield, a 15 pp decline in rates is assumed. The size of the shock is based on historical evidence. In the past, even bigger falls were experienced over a couple of months but at that time, the BSL did not have its overnight interest rate corridor in place which can serve as a floor for market interest rates.

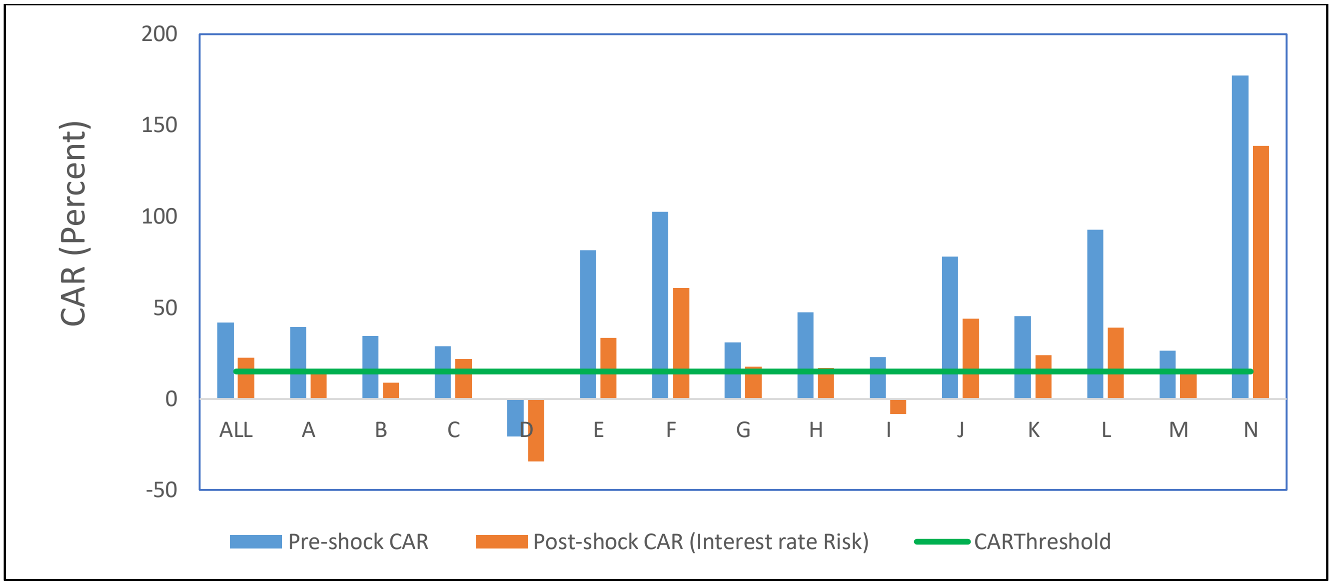
This situation may arise from positive events in the balance of payments, such as an improvement in the current account or a rise in foreign grants and official loans, which may prompt the government to reduce the number of domestic T-bills it issues. T-bills rates will therefore decline because of the subsequent decrease in T-bill supply, approaching the lower bound of the overnight interest rate corridor. Banks have the option to place their liquidity with the standing overnight deposit facility of the BSL, so they are expected to reject longer term investments below that rate plus some term spread.

Results of the Interest Rate Risk Stress Test

This risk scenario has a severe negative impact on banks since most banks hold sizable portfolios of Government T-bills, which generate enormous interest income for them and account for a sizable portion of their total revenue.

Nonetheless, the result of the stress test indicates that the banking sector as a whole is resilient to this interest rate shock, even though the post-shock CAR is significantly lower. The CAR declined to 22.6 percent from the pre-shock ratio of 41.8 percent but still remains above the prudential threshold (15 per cent). Individually, four banks breached the prudential floor although one of these had already breached the threshold before the shock (*Figure 3.1*).

Figure 3.1: Results of Interest Rate Shock



Source: FSD, BSL

In the above interest rate stress test, we tested the resilience of the banking sector to direct interest rate risk. Direct interest rate risk is the risk incurred by banks when there is a mismatch between the volumes of interest rate sensitive assets and liabilities. The test does not consider indirect interest rate risk although banks are exposed to it.[1]

3.2.3 Credit risk: recession

This scenario assumes an adverse situation where the Sierra Leone economy slips back into recession.

A recession would have negative effect on the credit risk of banks' loan portfolio. Three sub-scenarios are investigated to assess the impact of higher credit risk on banks' financial position, a proportional increase in NPLs, a sectoral shock and a large exposure shock.[2]

[1] Indirect interest rate risk is the risk arising from the impact of interest rate changes on the creditworthiness and ability of

[2] These sub-scenarios are qualitatively consistent with the narrative of the macro scenario, but they are not quantitatively derived from it.

Credit risk stress test scenarios

1) The NPLs increase uniformly across all banks by 40% and reach in aggregate more than 20 percent of total loans.

2) The sectors are affected in different ways, summarized in *Table 3.1* below.

Table 3.1: Assumed Sectoral Increase in NPL ratio*

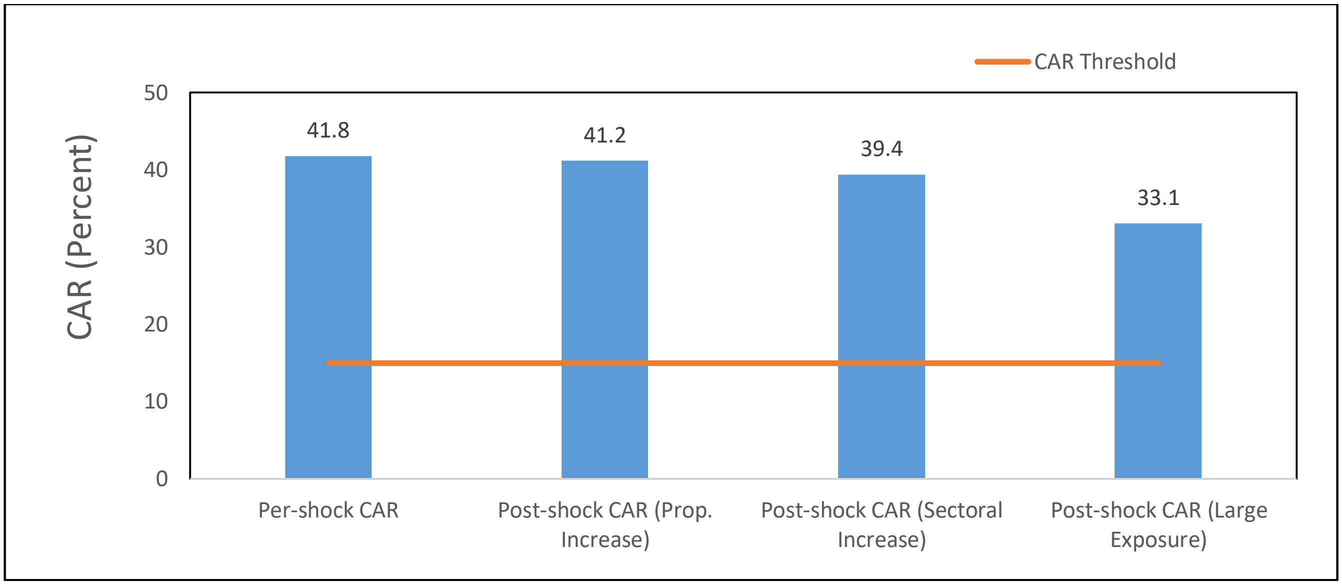
Sector	Shock
Commerce and Finance	60
Construction	50
Business Services	30
Personal Services	30
Manufacturing	20
Agriculture and Forestry	30
Transport and Storage	20
Utility Services	20
Communication	20
Petroleum	20
Others	20

* *Note: percentage of Performing Loans in the Sector Becoming NPLs*
Source: FSD, BSL

3) The 10 biggest loan of each bank defaults. Even though the international practice involves a lower number of defaulting loans, in Sierra Leone, some of the large lenders borrow from several banks at the same time. If one of the top five largest customers of a bank defaults, it is likely that the same customer will default on its other loans, which usually represent a top 10 loan for another bank.

The results of these stress tests indicate that the banking sector as a whole is resilient to credit risk based on all three tests. The current strong capital base of the banking sector was robust enough to absorb the impact of the shocks. Also, the impact of the shock itself is relatively small because of the low level of banks' loan relative to total assets. That said, the rise in NPLs varies quite a lot under these sub-scenarios especially under the large exposure scenario (see *Figure 3.2*).

Figure 3.2: Impact of Shocks on the Banking Sector CAR Ratio

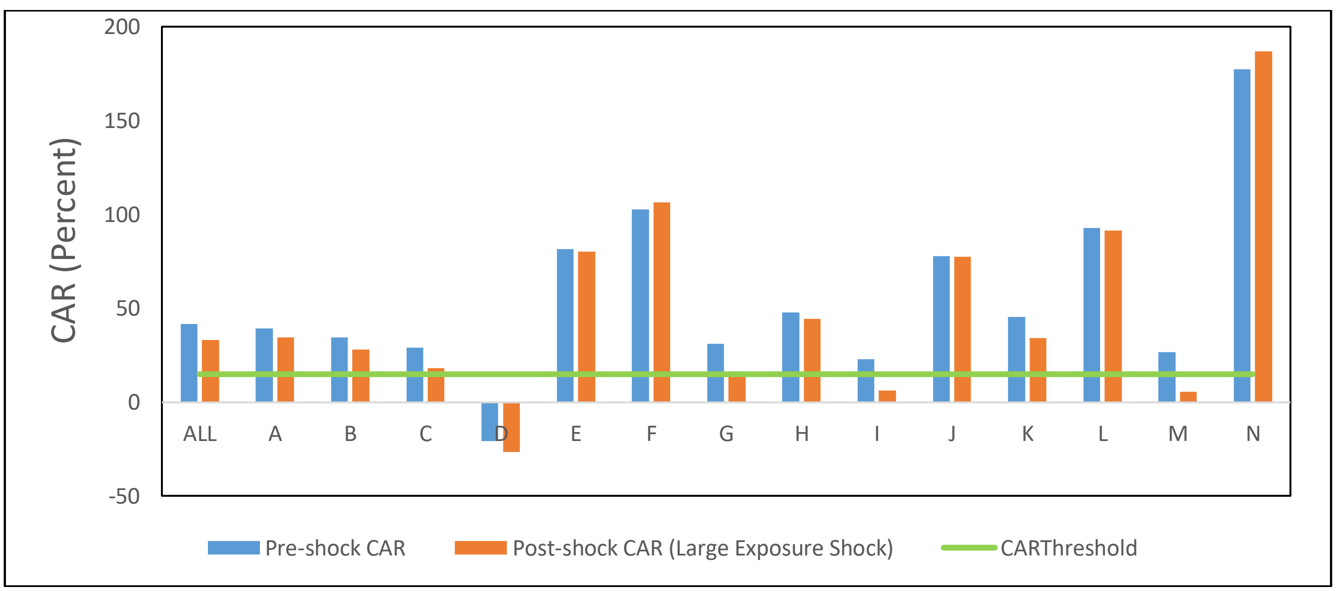


Source: FSD, BSL

3.2.3.1 Results of Large Exposure Stress Test

The banking sector CAR after the large exposure scenario declined a lot to 33 percent but still remained well above the prudential threshold of 15 percent. However, when we consider individual banks, the CARs of three banks fell below the prudential threshold of 15 percent (*Figure 3.3*). Banks with less holdings of government securities were more impacted by this shock, whilst banks with large holdings of government securities were insulated despite the extreme degree of the shock.

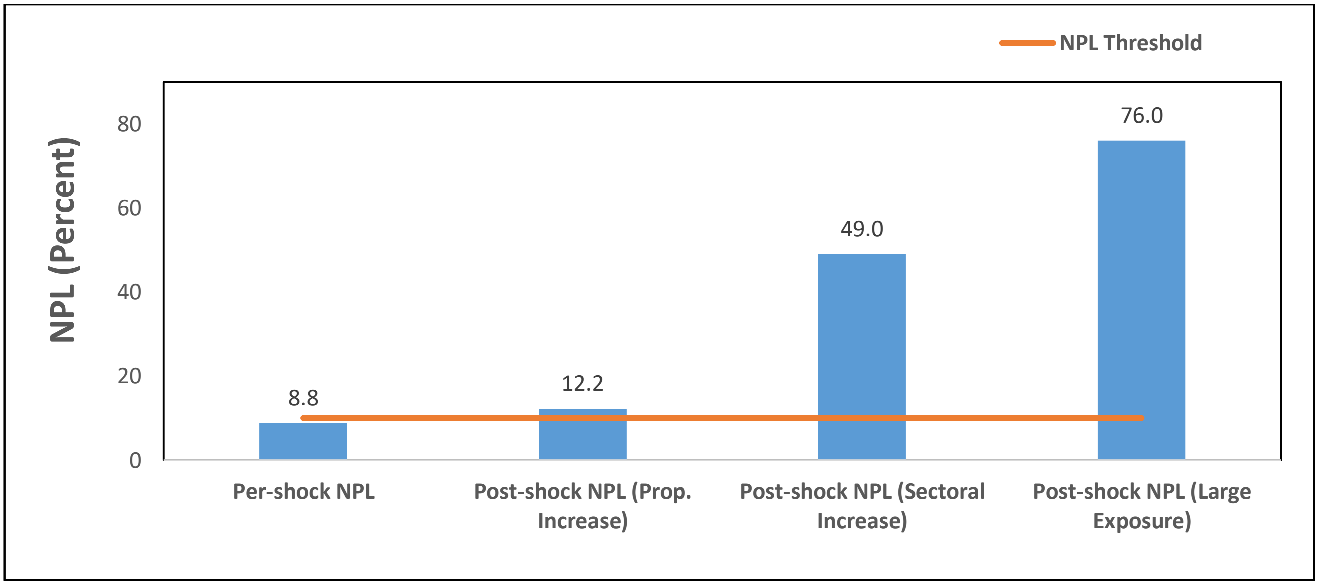
Figure 3.3: Impact on Individual Banks' CAR of the Ten Large Exposures becoming NPLs



Source: FSD, BSL

However, the impact on the banking sector's NPLs was significant, causing the NPLs to increase to 76.0 (*Figure 3.4*).

Figure 3.4: Impact of Large Exposure Shocks on the Banking Sector NPL Ratio



Source: FSD, BSL

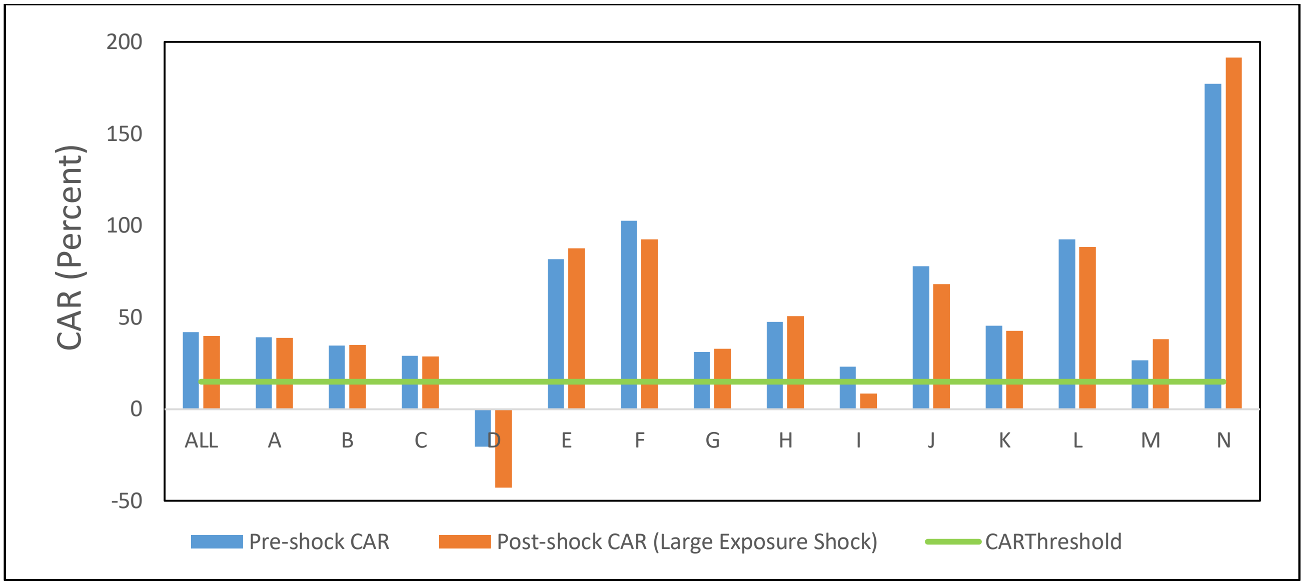
3.2.4 Foreign exchange rate risk: large depreciation

The foreign exchange risk is the risk that exchange rate changes affect the local currency value of financial institutions' assets, liabilities, and off-balance sheet items. In this test, we consider only the direct solvency risk arising from banks' net open positions (NOP) in foreign currency. The indirect solvency risk arising from the impact on the creditworthiness of foreign exchange loan borrowers was not considered since the banking sector cannot give out foreign currency loans as set out by regulation. Leone depreciation will have a positive impact on banks that have a long (positive) NOP in foreign currency and a negative impact on banks that have a short (negative) NOP. The assumption is that the Leone will depreciate by 50 per cent in the next 6 months.

3.2.4.1 Results of the Exchange Rate Stress test

The results show that the impact of the foreign exchange shock on the resilience of the banking sector was minimal given that in aggregate the sector had close to zero NOP. The banking system CAR declined only marginally to 40 percent. But individual banks' NOP differed significantly since eight recorded a long position and six reported a short position. Nonetheless, even for banks with a short position beyond the regulatory minimum, the impact of Leone depreciation is relatively small (*Figure 3.5*).

Figure 3.5: Impact on Individual Banks' CAR of a 50 Per cent Leone Depreciation



Source: FSD, BSL

3.2.5 The Combined Scenario: Recession and Financial Repression

This unfavorable scenario combines the recession scenario with the negative impact of fiscal policy tightening and exchange rate depreciation. It assumes that:

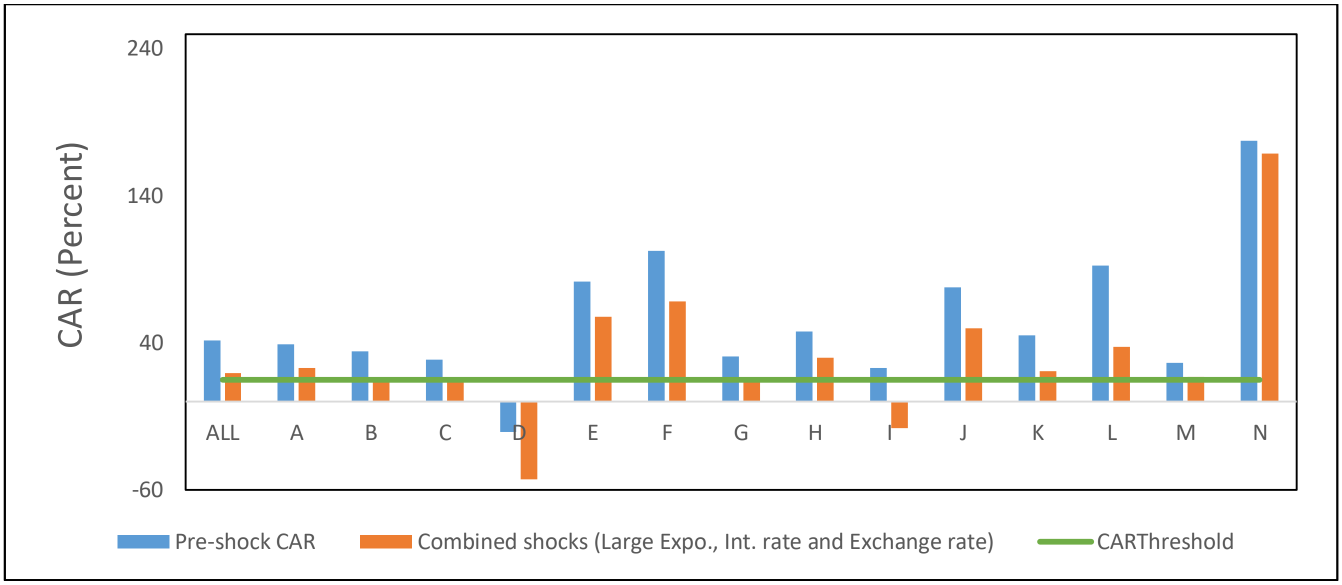
- 10 largest exposures in the banking sector default, yields on GSs fall by 15 percent and the Leone depreciates by 50%.

3.2.5.1 Results of the Combined Stress Test (Recession and financial repression)

The combined stress test was used to test the resilience of the banking sector to multiple shocks emanating from credit risk (large exposures), exchange rate depreciation and declining government security yields. The test adds up the impacts of multiple shocks to arrive at an aggregate impact on the CAR of the banking sector. The combined scenario is a low probability but conceivable event.

The results indicate that the banking sector as a whole withstands the combined shock although the aggregate CAR halves to 20 percent. When we consider individual banks, four banks recorded CAR below the 15 percent regulatory threshold with two recording a negative CAR. The CAR of ten banks remained above the regulatory limit of 15 percent (*Figure 3.6*). Still, the key takeaway is that such a combined adverse shock although weakening the banking sector would not cause a full-blown crisis.

Figure 3.6: Impact on Individual Banks' CAR of the Combined Stress Scenario Test



Source: FSD, BSL

3.2.6 Liquidity risk

Two different liquidity stress scenarios are used in the stress testing exercise. The impact of the liquidity stress scenarios is calculated for each bank in terms of the number of days it would be able to survive without resorting to liquidity from outside (other banks or the central bank). Of course, in real life the central bank may very well intervene through its lender-of-last-resort function.

Liquidity scenarios

First scenario: It affects all banks in the system proportionally (similar run on all banks) depending on their volumes of demand and time deposits. The scenario assumes that banks endure a daily withdrawal from LCY demand deposits, FX demand deposits, LCY time deposits and FX time deposits of 25, 15, 25 and 5 percent, respectively.

Second scenario: It stands for "flight to safety," where the liquidity drain starts in the smallest or weakest banks and the stress test shows how this can affect the larger or stronger banks. The stress test investigates three possible measures of "bank safety": (i) total assets; (ii) total assets, with a premium for state ownership; and (iii) the public assessment of the banks' quality, proxied by the BSL's own internal rating. In the first case, depositors perceive bank safety as linked to the size of the bank, approximated by total assets. In the second case, they also perceive state-owned banks safer than privately-owned banks (because of an explicit or implicit government guarantee in the former case). In the third case, depositors' perceptions of bank safety are correlated with the banks' recent financial performance proxied during the stress testing exercise by the BSL's own rating.

The second scenario assumes that banks endure a daily deposit withdrawal from LCY demand deposits, FX demand deposits, LCY time deposits and FX time deposits ranging from 0 to 25, 15, 25 and 5 percent, respectively. For each bank, the size of the withdrawal within that range depends on its perceived safety.

For both scenarios, on any given day banks can utilize 75 percent of their outstanding liquid assets and 1 percent of their non-liquid assets. The liquidity scenarios are evaluated over a five-day horizon, corresponding to a week in calendar terms.

3.2.6.1 Liquidity Stress Test Results

The simple test models a liquidity drain that affects all banks proportionally, depending on their volumes of demand and time deposits (see the Box above for details). This assumes that customers do not switch deposits from one bank to another but rather reduce deposits from all domestic banks. The result of the simple liquidity stress test indicates that no banks will be illiquid after the first day, three after the second day, four banks after the third day and five banks after the fourth day. As the assumed liquidity drain are extremely large and, in practice, the BSL's liquidity facilities would be available to the banks, the results suggest only a moderate overall liquidity risk (*Table 3.2*).

The flight to safety test is based on "liquidity contagion" and assumes that a relatively large liquidity drain starts in the smallest or weakest banks and the impact of this effect on the larger or stronger banks is tested. That is, banks' customers consider stronger banks as safer than weaker banks. According to the flight to safety liquidity test, only two banks will become illiquid after the second day. The number of illiquid banks increases to three on the third day, five on the fourth day and six on the fifth day (*Table 3.2*). As the liquidity drain assumptions are even more severe than in the case of the simple test and as the liquidity drain affects the weaker banks disproportionally more under this scenario, the results are in line with expectations. However, the affected banks should take action to improve their liquidity positions.

Table 3.2: Simple Liquidity Stress Test Results

Days after shock	Number of illiquid banks	
	Run on all banks	Flight to safety/contagion
After day 1	0	0
After day 2	3	2
After day 3	4	3
After day 4	5	5
After day 5	7	6

Note: The assumed shock is 20 percent daily withdrawals of deposits for five days
Source: FSD, BSL

3.3 Conclusion and Recommendations

In summary, the stress tests show that the banking sector is generally resilient to large adverse shocks that might emerge in the future. A combination of such large shocks would certainly weaken the banking sector but would not be expected to result in a full-blown crisis. None of the individual macro shock scenarios considered would cause the sector's CAR to fall below the 15 percent minimum threshold. The reason for this is that most banks are starting with very high levels of CAR emanating from their unique business models, which is based on large holdings of government securities that are considered for regulatory purposes as risk free and provide very high returns. Therefore, even with extreme shocks to credit risk, the banking sector's CAR continues to remain adequate. However, the BSL will consider placing a higher weight on alternative financial stability indicators, such as the leverage ratio, as the risk-weighted assets is significantly biased by the large government security portfolios of the banks, which may not be sustainable over the long run.

Vulnerabilities do exist in the banking sector which arise mainly from a few weak banks in the sector. However, these banks are already under enhanced supervision. The BSL will consider whether additional banks should be put under enhanced supervision. Thus, the following recommendations are proffered to strengthen the banking sector and reduce its vulnerabilities.

- Prompt steps should be taken to strengthen the bank that has already breached the regulatory capital threshold.

- The BSL will prepare new rules on credit reporting so that banks will need to provide more details when reporting credit information. It will be of great value if a breakdown is also provided on borrowing by the government, individuals, non-profit organizations, corporate and non-corporate businesses etc.
- The BSL encourages banks to improve their capital base over time to increase resiliency to shocks as they diversify their asset portfolio. The BSL will use its available tools for the purpose.
- Even though the stress test results on foreign exchange risk show that the impact of an exchange rate shock is minimal, foreign exchange risk can easily transform into credit risk once banks start lending in foreign currency to their customers whose original hedged position may change substantially over time. Therefore, the Financial Policy Committee of the Bank will consider the introduction of additional macroprudential tools to manage foreign exchange risks.

4 NON-BANK FINANCIAL SECTOR

4.1 Other Financial Institutions

4.1.1 Landscape

The Other Financial Institutions' (OFIs) landscape remained little changed in 2023. The number of Deposit Taking Microfinance Institutions (DTMFIs), Community Banks (CBs), Financial Services Association (FSA), Mobile Money Operators (MMOs) and Discount Houses (DHs) remained unchanged. The number of Credit-Only Microfinance Institutions (COMFIs) increased to sixty-nine whilst the number of Credit Unions (CUs) fell slightly to twenty-five (*Table 4.1*).

Table 4.1: Structure of other Non-bank Financial Institutions

Institutions	Number		Foreign owned		Number of branches		Number of employees		Concentration ratio* (%)	
	2022	2023	2022	2023	2022	2023	2022	2023	2022	2023
Deposit Taking Microfinance Institutions	5	5	2	2	67	67	794	789	97.36	97.56
Credit-Only Microfinance Institutions**	60	69	2	2	122	128	1,101	1,247	70.33	74.39
Community Banks***	17	17	Nil	Nil	23	23	169	169	39.53	29.29
Financial Services Associations	59	59	Nil	Nil	59	59	198	198	12.61	13.67
Mobile Money****	3	3	3	3	48,087	72,454	105	105	N/A	N/A
Discount Houses (DHs)	2	2	Nil	Nil	2	2	21	30	69.56	59.71

* *Concentration = Assets of 3 largest /Total Assets, (DHs: Assets of 1 large/Total Assets)*
** *39 out of 69 COMFIs submitted returns as of October 2023*
*** *17 Community Banks plus 6 Cash Points*
**** *Mobile Money = No. of Agents, not branches.*
Source: OFISD, BSL

4.2 Deposit-Taking Microfinance Institutions (DTMFIs)

4.2.1 Activity of DTMFIs

The DTMFIs continued their expansion in terms of assets, equity, deposits, and loans, but their growth remained much lower than the inflation rate, representing sizeable decline in real terms (*Table 4.2*). The sector exhibited significant reduction in concentration, with the largest DTMFI accounting for 37 percent of the sector's assets at the end of 2023, compared to 42 percent at the end of 2022.

Table 4.2: Activities of the DTMFIs

Deposit-taking Microfinance Institutions	2022	2023
Total Assets (NLe million)	577	761
Total Deposits (NLe million)	229	255
Total Loans (NLe million)	310	370
Total Equity (NLe million)	133	157
Interest Rate on Loans (average) Percent	30	30
Interest rate on Deposits (average) Percent	3-5	3-5
Number of Clients (000s)	70	66

Source: OFISD, BSL

4.2.2 Performance of DTMFIs

DTMFIs' profits increased by 30 per cent. As their total assets increased faster, the ROA decreased slightly to 2.4 percent. On a consolidated basis, the ROA exceeded the minimum MIX standard of 2.1 percent but on an individual basis, two (2) of the five (5) DTMFIs did not meet the minimum standard. ROE on a consolidated basis fell to 11.6 per cent below the MIX benchmark of 13.6 percent with three (3) of the five (5) DTMFIs recorded ROE below the MIX benchmark.

Table 4.3: Selected Performance Indicators for DTMFIs

Deposit-Taking Microfinance Institutions	2022	2023
Income:		
Interest Income (Le million)	83	107
Expenditures:		
Interest Expense (Le million)	24	36
Personnel and Administrative Expenses (Le million)	78	102
Net Profit		
ROA (Net Income/Total Assets), in %	3.0	2.4
ROE (Net Income/Capital), in %	13.3	11.6
Non-Performing Loans (NPL), in % (PaR)	12.7	13.1

Source: OFID, BSL

The Portfolio at Risk (PaR) ratio increased to 13 percent with all DTMFIs failing to meet the maximum MIX standard of 4.8 percent. The BSL will continue to engage the DTMFI's to help improve their credit management practices and loan recovery strategy to decrease their PaR. Also, more attention will be given to on-site examinations for institutions that are recording higher PaR above the industry average.

4.3 Credit-Only Microfinance Institutions (COMFIs)

4.3.1 Activity of COMFIs

Both the total assets and loans of reporting COMFIs increased by 30 percent in 2023 (*Table 4.4*). However, only thirty-nine of the sixty-nine firms in the industry submitted returns. The BSL will continue to levy sanctions, or consider more severs steps, on the non-complying institutions to force them to submit the required returns.

Table 4.4: Activity of COMFIs*

Credit-only Microfinance Institutions	2022	2023
Total Assets *(NLe million)*	487	634
Total Loans *(NLe million)*	349	453
Total Equity *(NLe million)*	181	153
Interest Rate on Loans (Average) *percent*	25-30	30-35
Number of Borrowers (000s)	274	506

Source: OFISD, BSL

**Note: The figures across years are not comparable as 36 out of 60 institutions reported in 2022, while 39 out of 69 COMFIs submitted returns in December 2023. Also, not all institutions that reported in December 2022 may have reported for December 2023.*

4.3.2 Performance of COMFIs

COMFIs in aggregate made a loss in 2023 with 10 individual firms making significant losses.

Table 4.5: Selected performance indicators of COMFIs

Credit-only Microfinance Institutions	2022	2023
Income:		
Interest Income (NLe million)	166	207
Expenditure		
Interest Expense (NLe million)	22	28
Personnel and Administrative Expenses (NLe million)	103	185
Net profit/Loss		
ROA (Net Income/Total Assets, in Percent	11.0	(2.4)
ROE (Net Income/Capital), in Percent	29.0	(9.7)
Non-Performing Loans (NPL), in Percent (PaR)	11.7	7.2

Source: OFISD, BSL

4.4 Community Banks (CB)

4.4.1 Activity of Community Banks

The CBs' total assets increased by 15 percent reflecting mainly rapid growth of investments. Concentration remained high in the sector with the three largest CBs accounted for 39 percent of total assets.

Table 4.6: Activity of Community Banks

Community Banks	2022	2023
Total Assets (*NLe'000*)	162,341	186,120
Total Loans *(NLe'000*)	89,896	103,633
Total Deposits (*NLe'000*)	75,991	84,195
Total Equity (*NLe'000*)	63,898	78,131
Interest Rate on Loans (*Average*; *Percent)*	24	30
Number of borrowers	41,960	42,331
Number of depositors	119,803	113,812

Source: OFISD, BSL

4.4.2 Performance of Community Banks

Overall, the profitability of the CB sector increased by 9 percent with NPLs continuing to decrease. ROA and ROE fell slightly from the previous year but remained above their respective MIX standards.

Table 4.7: Selected Performance Indicators of Community Banks

Community Banks	2022	2023
Income:		
Interest Income (NLe million)	24	25
Expenditures:		
Interest Expense (NLe million)	1.0	0.6
Operating Expenses (NLe million)	18	21
Net Profit:		
ROA (Net Income/Total Assets), in Percent	8.1	7.6
ROE (Net Income/Capital), in Percent	14.3	13.6
Non-Performing Loans (NPL), in Percent (PaR)	16.1	14.0

Source: OFISD, BSL

The PaR fell to 14.0 percent but was still far above the minimum MIX standard of 4.8 percent.

4.5 Financial Services Associations (FSAs)

4.5.1 Activities of Financial Services Associations

FSAs' total assets and gross loans fell by 2 per cent and 9 per cent respectively. The loan portfolio quality also declined significantly with the PaR increasing to 26.7.

Table 4.8: Activity of the Financial Services Associations (FSAs)

Financial Services Associations (FSA)	2022	2023
Total Assets *(NLe million)*	92	90
Share Capital *(NLe million)*	28	30
Total Loans *(NLe million)*	64.7	58,9
Number of Active Loan Clients (000s)	34.3	28.5

Source: OFISD, BSL

4.5.2 Performance of Financial Services Associations

Financial Services Associations (FSAs) exhibited a satisfactory, albeit somewhat deteriorating, performance. Total income fell slightly (by 2 percent) driven mainly by a decline in interest income. With personnel and administrative expenses increasing more rapidly, profitability decreased by 20 percent.

Table 4.9: Selected Performance Indicators of FSAs

Financial Services Association	2022	2023
Income:		
Interest on Loan Income *(NLe)*	14.3	13.3
Expenses:		
Financial Expense *(NLe million)*	1.7	1.4
Admin Expenses and Personnel Expenses *(NLe million)*	9.3	10.2
Efficiency Ratios:		
ROA (Net Income/Total Assets) Percent	7.1	3.9
ROE (Net Income/Capital) Percent	17.0	6.9
Non-Performing Loans (NPL) Percent	11.0	26.7

Source: OFISD, BSL

4.6 Mobile Money Operators (MMOs)

4.6.1 Activity of the Mobile Money Operators

MMOs experienced significant increases in their number of agents, accounts and number and value of transactions (*Table 4.10*).

Table 4.10: Activities of the Mobile Money Providers

Activity of MMOs	2022	2023
Number of Agents (000s)	48.1	72.4
Number of Accounts (millions)	7.8	8.2
Number of Active Accounts (millions)	1.4	1.8
Number of transactions (millions)	92.1	128.6
Value of transactions (NLe billions)	19.9	39.2

Source: OFISD, BSL

4.7 Discount Houses (DHs)

4.7.1 Activity of DHs

Total assets almost halved during the year.

Table 4.11: Activities of DHs*

Discount Houses	2022	2023
Total Assets *(NLe millions)*	48.3	25.4
Placement (Deposits) *(NLe millions)*	1.3	0.8
Share Holders Funds *(NLe millions)*	11.2	9.0
Investment in Gov't Securities (*NLe millions*)	5.9	6.5
Loan (Repo) (*NLe millions*)	2.3	1.7

Source: OFISD, BSL
Note: The total liabilities figures of NLe37.10 and NLe16.39 in 2022 and 2023 respectively excluded the Share Holders' Funds for those periods.

4.7.2 Performance of Discount Houses (DHs)

Pre-tax profits were flat on the year but ROA and ROE both rose modestly (*Table 4.12*). However, the cost-to-income ratio increased somewhat (to 80 percent).

Table 4.12: Selected Performance Indicators of DHs

Discount Houses	2022	2023
Income:		
Discount Income (NLe million)	1.1	1.5
Operating Income (NLe million)	0.9	1.5
Expenses:		
Interest Expense (NLe'000)	11	21
Operating Expenses (NLe'000)	1,471	2,360
Earnings:		
Current year profit (NLe'000)	597	602
ROA (Net Income/Total Assets, in Percent	1.3	1.6
ROE (Net Income/Capital), in Percent	4.3	4.5
Operating Expenses/Operating Income (Percent)	261.14	155.78

Source: OFISD, BSL

4.8 Apex Bank (SL) Limited (ABSL)

4.8.1 Activity of ABSL

The balance sheet of ABSL shrunk during the year whilst the PaR increased significantly to 45 percent. Allowances for loan losses remained the same even though there were a marked increase in NPLs.

4.8.2 Performance of Apex Bank (SL) (ABSL)

ABSL recorded a pre-tax loss with modest growth in gross financial income (5.0 percent) significantly outweighed by rapid growth in operating expenses (38 per cent). The ROA and ROE were both negative, recording minus 3.60 percent and minus 9.17 percent respectively.

4.9 Credit Unions (CUs)

4.9.1 Financial Condition and Performance of CUs

As of December 2023, the total number of CUs decreased to twenty-five (25) from twenty-seven (27) in December 2022. Notwithstanding the decrease in the total number of CUs, total membership increased by 1,787 members, a 12.15 percent increase, to 16,494 members in December 2023. The consolidated total assets of the CU sector increased by NLe5.68 million to NLe30.04 million in December 2023 compared to NLe24.36 million in December 2022. Total savings increased to NLe19.60 million in December 2023 from NLe15.31 million in December 2022. Share capital and gross loans increased by

43.60 percent and 14.73 percent recording NLe3.69 million and NLe20.97 million, respectively, as of December 2023.

4.10 Foreign Exchange Bureaux (FEB)

4.10.1 Purchases and Sales of Foreign Currencies

The foreign currency market revealed that the US dollar remains easily the dominant currency in the foreign exchange market (*Table 4.13*).

Table 4.13: Purchases and Sales of Major Foreign Currencies for FXBs

Details	**Dec-22**		**Dec-23**	
	Purchases	**Sales**	**Purchases**	**Sales**
USD ($), 000s	**3,092**	**1,735**	**1,381**	**1,361**
GBP (£), 000s	**129**	**19**	**62**	**81**
EURO (€), 000s	**25**	**22**	**2**	**-**

So1urce: OFISD, BSL

Currently, there are twelve (12) Foreign Exchange Bureaux operating as Super Agents dealing directly with International Money Transfer Organizations (IMTOs). However, twenty-three Foreign Exchange Bureaux have been granted a “No Objection” to do inward remittances.

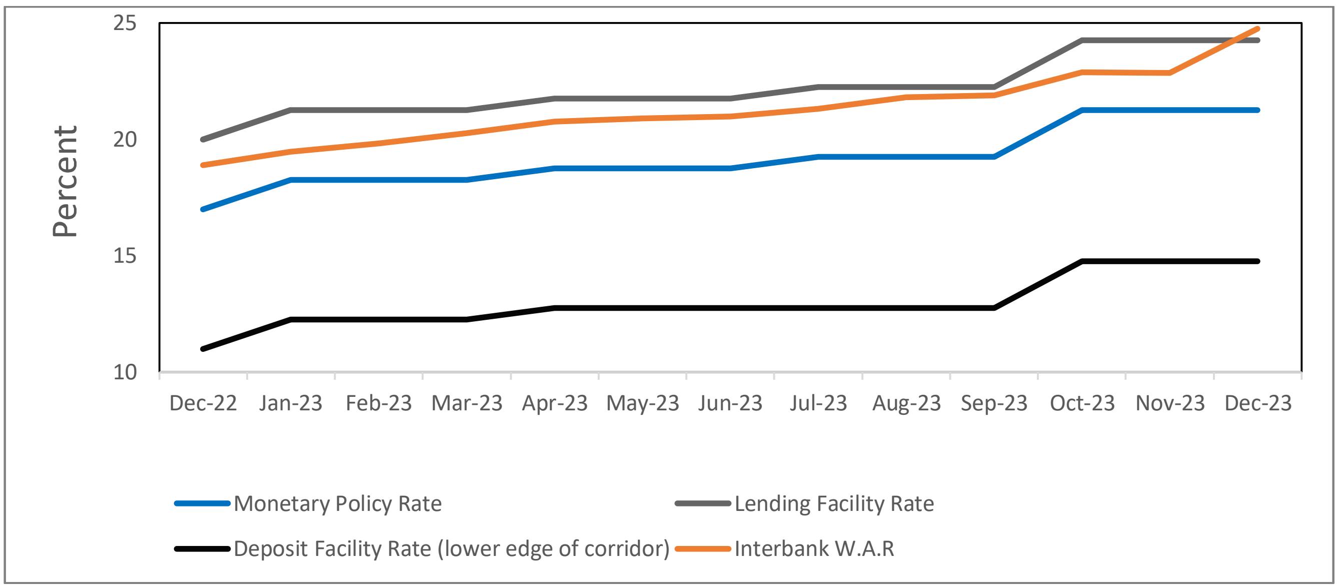
Total inward remittances of USD slightly declined in the year to $39.7 million. This decline could be attributed to a slowdown in economic activity due to the political instability that took place towards the end of the year.

5 DEVELOPMENTS IN MONETARY POLICY IMPLEMENTATION AND THE MONEY MARKET

5.1 BSL liquidity operations

The Bank increased its monetary policy rate (MPR) gradually by 525 basis points during 2023 (**Error! Not a valid bookmark self-reference.**). The overnight (O/N) standing lending facility (SLF) rate was increased by the same margin to 25.25 percent, while the O/N standing deposit facility (SDF) rate was only increased by 475 basis points to 15.75 percent. The SLF and SDF serve as the upper and lower limits respectively of the BSL's O/N interest rate corridor.

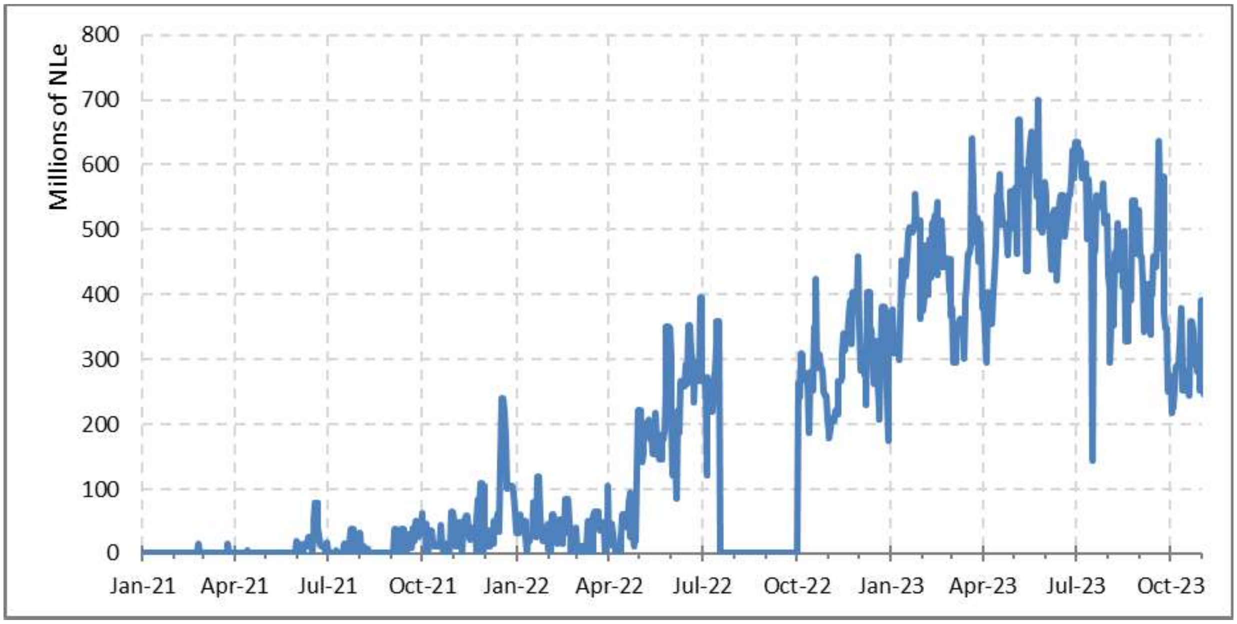
Figure 5.1: BSL Policy Rates and Interbank Weighted Average Rate (monthly)



Source: FMD, BSL

The BSL managed to aggregate banking sector liquidity in 2023 mainly through its open market operations (OMOs) and its O/N SLF. Access to the SLF window increased in the first half of 2023 and started to trend downwards after July 2023. At the end of 2023, access to the SLF was roughly the same as at the beginning of the year (**Error! Not a valid bookmark self-reference.**). The banks did not use the O/N standing deposit facility (SDF) window, consistent with the continued tight liquidity situation.

Figure 5.2: Outstanding stock of the BSL's O/N SLF (daily)



Source: FMD, BSL

On the other hand, the Bank's intervention in the secondary market through outright purchases of treasury bills increased by 64 percent from NLe3.6 billion as of December 2022 to NLe5.9 billion as of December 2023.

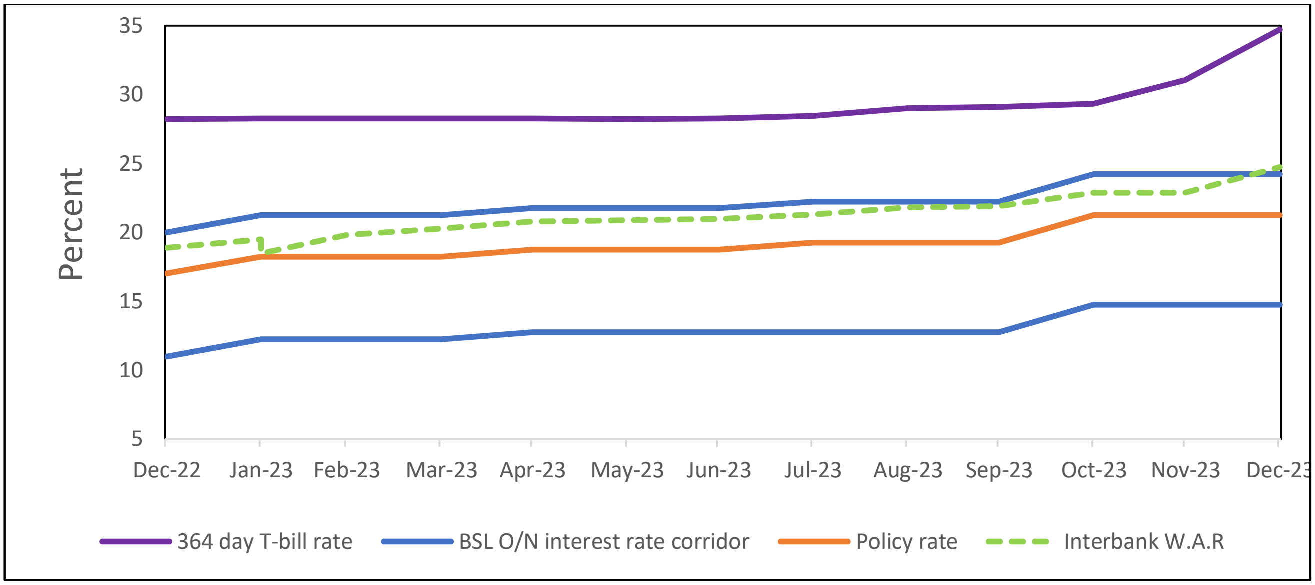
5.2 Interbank market

The interbank money market in Sierra Leone is a market for dealing with liquidity surpluses and shortages between banks on a secured basis, mostly using repos. The interbank weighted average yield increased by 6 pp during 2023 reflecting mainly the tightening in the monetary policy stance (*Figure* 5.3).

Monthly interbank market turnover was similar to the previous year but the volume of transactions fell in real terms (Source: FMD, BSL

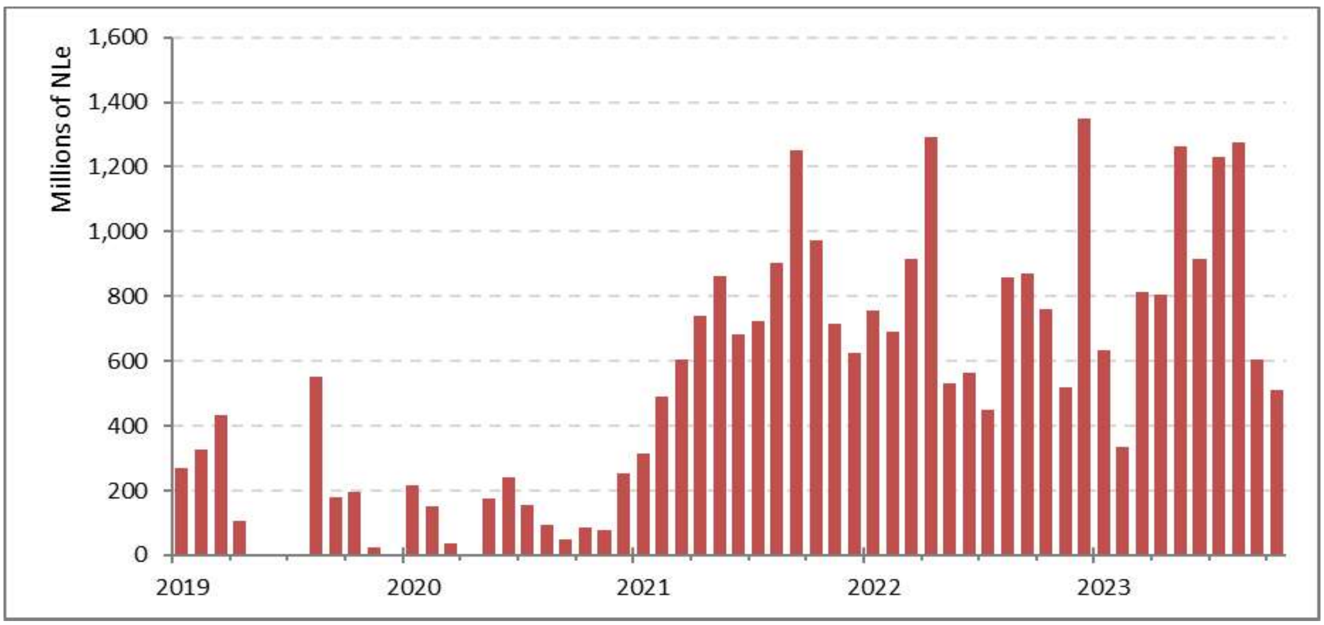
Figure 5.4).

Figure 5.3: BSL Policy Rates, the Interbank Rate and the 364-day T-bill rate (monthly)



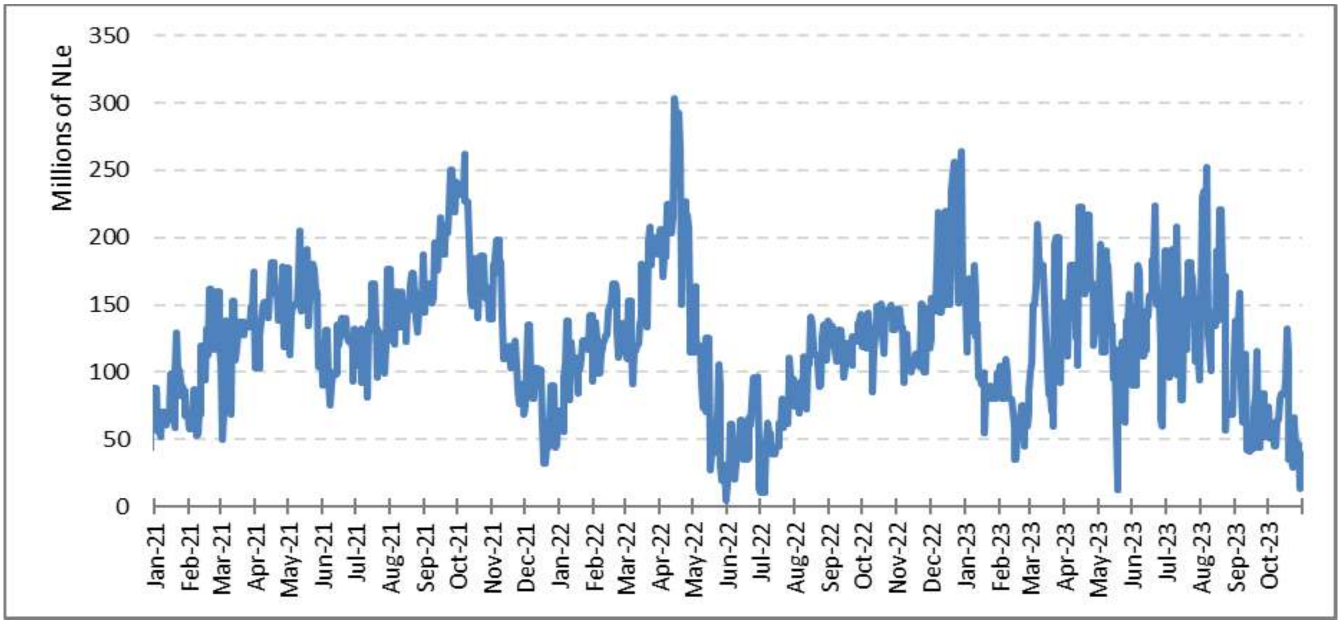
Source: FMD, BSL

Figure 5.4: Monthly Turnover in the Interbank Money Market



Source: FMD, BSL

Figure 5.5: Outstanding Amount of Interbank Loans (daily)



Source: FMD, BSL

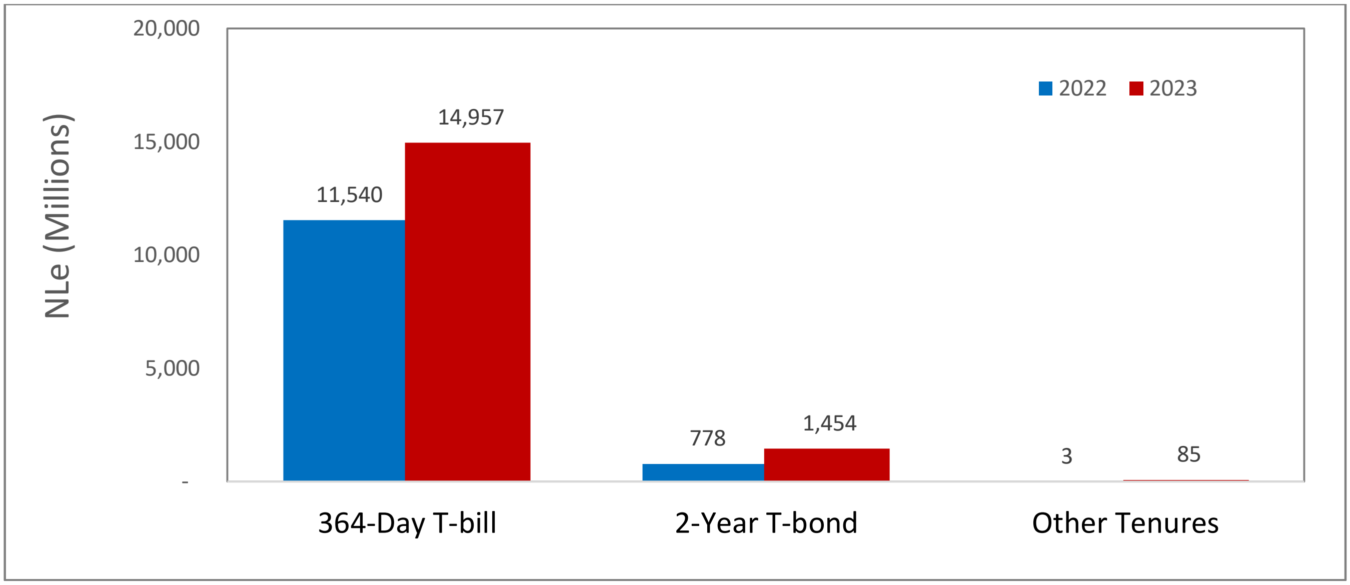
5.3 Government securities market

The Government Securities (GS) secondary market remained illiquid in Sierra Leone, as investors typically hold GS until maturity.

The primary market of GS comprises weekly auctions of 91-day, 182-day and 363-day T-bills. The 91-day and 182-day T-bill auctions are unattractive as these are usually and significantly undersubscribed, with often no single bid submitted.[3] In contrast, the 364-days tenure was mostly oversubscribed with commercial banks the main buyers. Less frequently, there are also auctions for longer term government bonds.

[3] Therefore, data on yields and volumes of these auctions are irrelevant from monetary policy or financial stability perspective.

Figure 5.6: Stock of Marketable Government Securities by Tenure

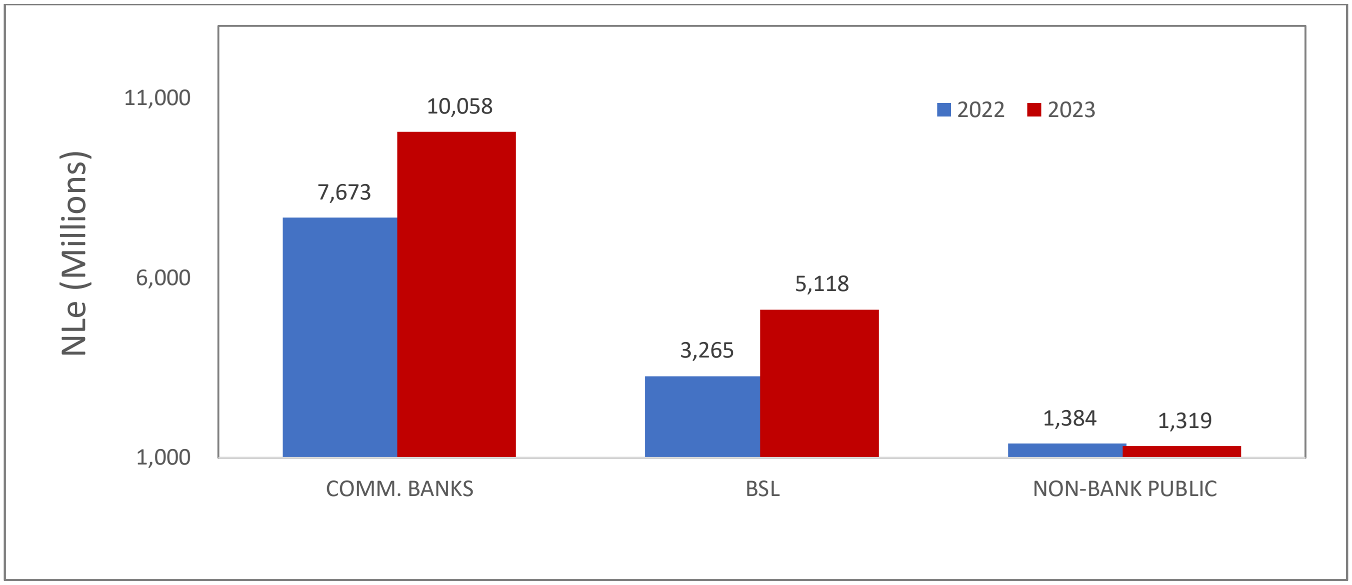


Source: FMD, BSL

The total stock of GS increased by 34 percent. Marketable securities accounted for almost 90 percent of the total, and these mainly served to finance the budget. The remainder, non-marketable securities, are mainly for financing specific infrastructural projects.

The commercial banks and the BSL increased their stock of GS by 35 percent and 46 percent respectively, whilst the non-bank public sector's holdings marginally declined by 1.7 percent as of December 2023. Commercial banks continued to be the largest investors. The increase in the BSL's holding was largely due to its outright purchases of Treasury Bills from the commercial banks to support aggregate liquidity in the money market.

Figure 5.7: Holdings of Marketable Government Securities by Sector (in Millions of New Leones)



Source: FMD, BSL

The 364-day treasury bill yield increased by 112 basis points during the year – significantly less than inflation (Figure 5.3).

5.4 Implications for Financial Stability

The developments in the Bank of Sierra Leone's (BSL) monetary policy and money market operations present several key implications for financial stability. The increase in the monetary policy rate (MPR) by 525 basis points in 2023, along with adjustments to the Standing Lending Facility (SLF) and Standing Deposit Facility (SDF) rates, reflects a tightened monetary stance aimed at managing inflation and stabilising the exchange rate. While this may help in controlling inflation, the rise in borrowing costs places additional pressure on commercial banks, particularly those reliant on short-term funding, potentially limiting private sector lending and affecting economic growth.

The BSL has managed overall banking liquidity through open market operations (OMOs) and SLF, though liquidity remains constrained. A reduction in SLF access since mid-2023 shows improved self-sufficiency in banks but highlights existing liquidity constraints. The lack of usage of the SDF indicates limited excess liquidity, which could pose liquidity risks for certain banks, possibly leading to more interbank borrowing or asset sales to cover funding needs.

Interbank market dynamics have also been impacted, with an increase in interbank yields reflecting the BSL's tightening stance. This rise in borrowing costs and limited transaction volumes present further challenges for banks facing liquidity shortages.

The government securities (GS) market remains largely illiquid, with a strong reliance on 364-day Treasury bills, often oversubscribed by commercial banks. This reliance could pose liquidity risks, as limited market depth may affect the GS market's role in stabilising financial stress. Furthermore, the increase in GS holdings by the BSL and commercial banks underscores their reliance on these assets, but such concentration may expose banks to interest rate risks and crowd out private sector credit, potentially constraining economic growth.

The moderate increase in 364-day T-bill yields poses an additional risk if inflation pressures persist. Investors may seek higher yields, thus raising government financing costs and potentially impacting banking sector stability.

The cumulative effects of high interest rates, limited liquidity, and reliance on GS holdings test the resilience of the banking sector amid economic uncertainties. The BSL's commitment to monitoring liquidity risks, enhancing interbank market flexibility, and promoting a more liquid GS market, combined with strengthened regulatory oversight and stress testing, will be critical in supporting financial stability and ensuring adequate capital buffers to withstand potential shocks.

6 NATIONAL PAYMENTS SYSTEM

6.1 Introduction

The BSL monitors and evaluates the Financial Market Infrastructure to attain efficiency and safety, given its significance.

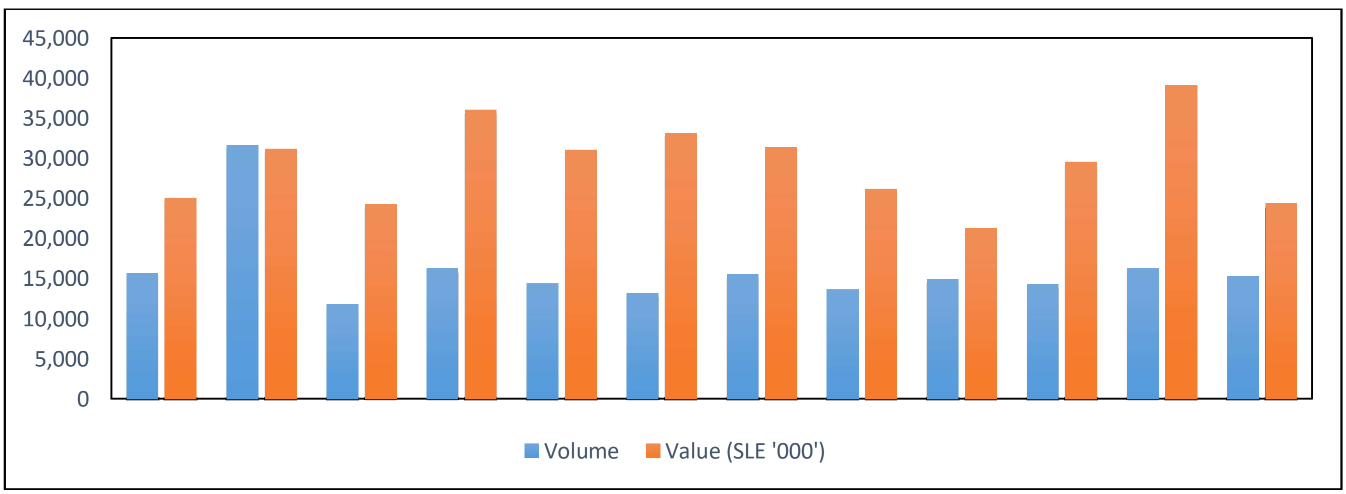
6.2 National Payments System Landscape

The Payment System in Sierra Leone continues to be dual with the coexistence of cash and non-cash transactions. The promotion of financial inclusion, safeguarding the environment of payment systems, and working with key stakeholders remained part of the BSL's three main priorities.

6.2.1 Real Time Gross Settlement (RTGS) system

The RTGS is an electronic funds transfer system for the settlement of payments across the country. Through the RTGS, transactions are settled, and funds can be transferred between participating financial institutions promptly.

Figure 6.1: Volume and value of RTGS transactions January-December 2023



Source: Banking Department, BSL

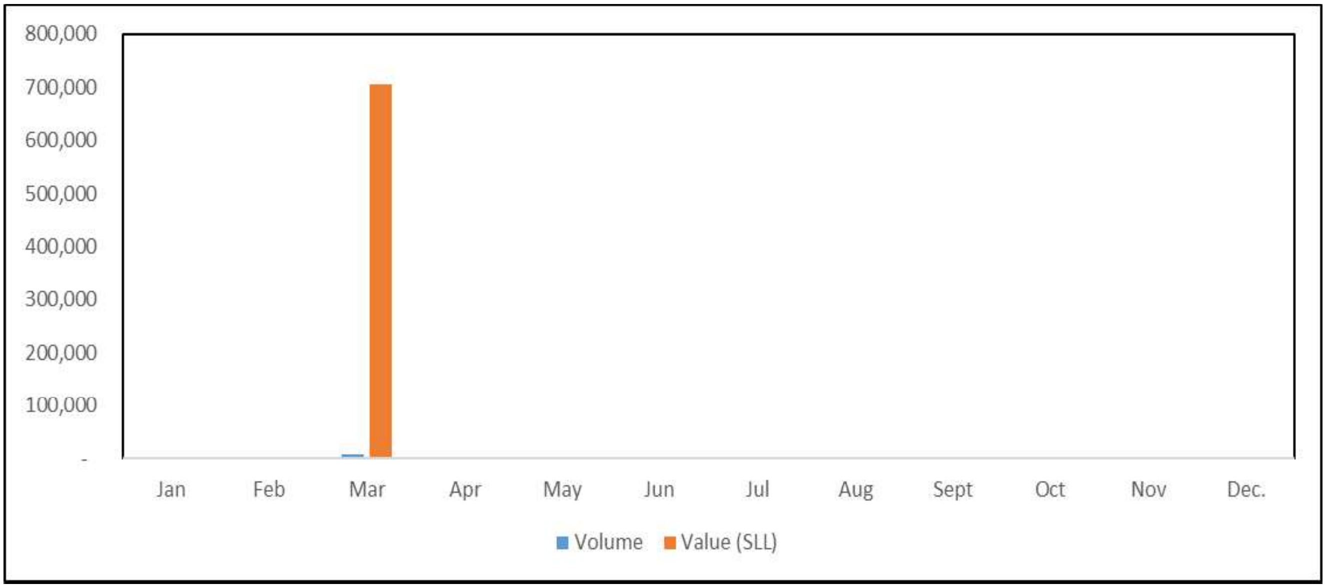
Even though the amount and value of transactions fluctuated, the trend revealed that the system was generally accepted for interbank transactions.

6.2.2 Automated Clearing House (ACH)

The ACH hosts the retail payment system, and it handles a large volume of cleared paper-based and electronic payments. Prior to the Leone's redenomination, most ACH transactions were high-volume, low-value retail payment cheques (less than fifty million Leones). To deter over-the-counter cash transactions, the cheques limit was eliminated in July 1, 2022.

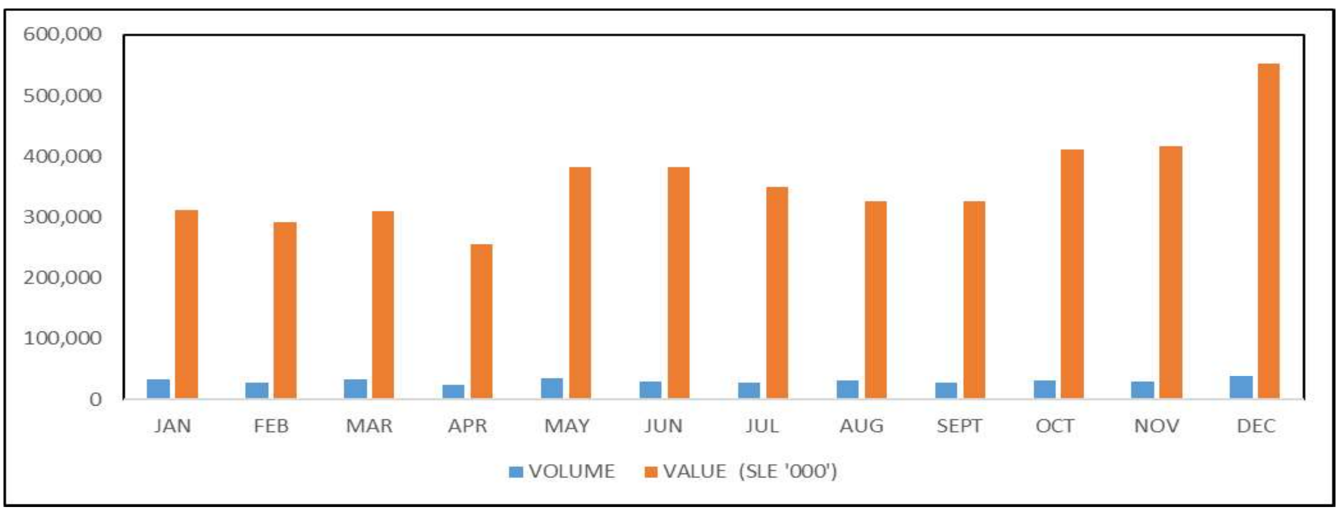
The charts below demonstrate that cheques continued to be used for more transactions than direct credit during 2023.

Figure 6.2: Direct Credit (SLL) Transactions January-December 2023



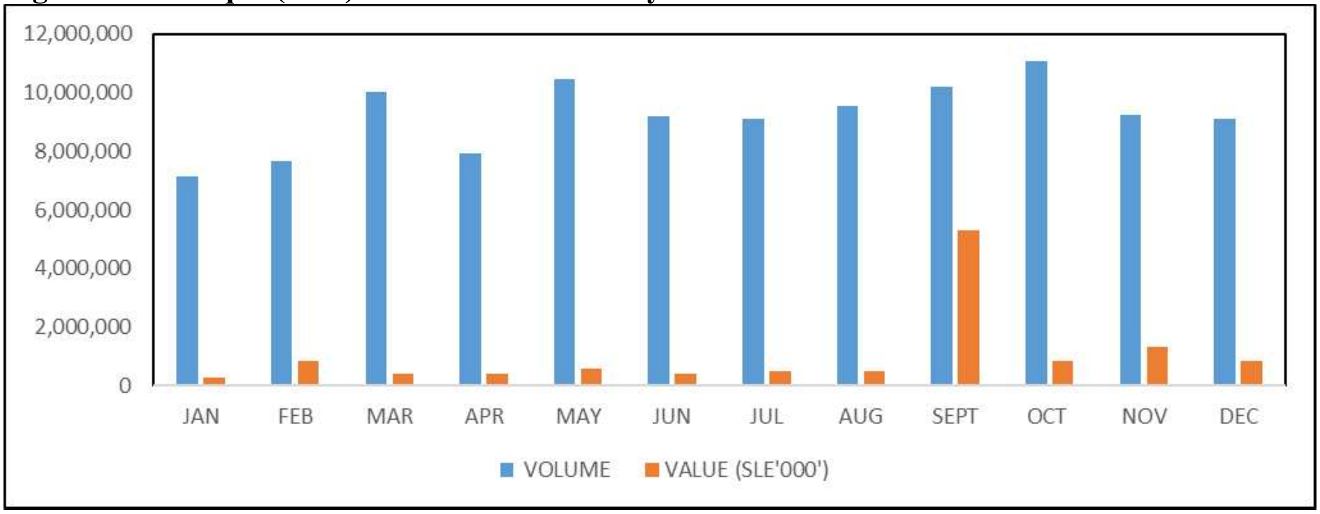
Source: Banking Department, BSL

Figure 6.3: Direct Credit (SLE) Transactions January-December 2023



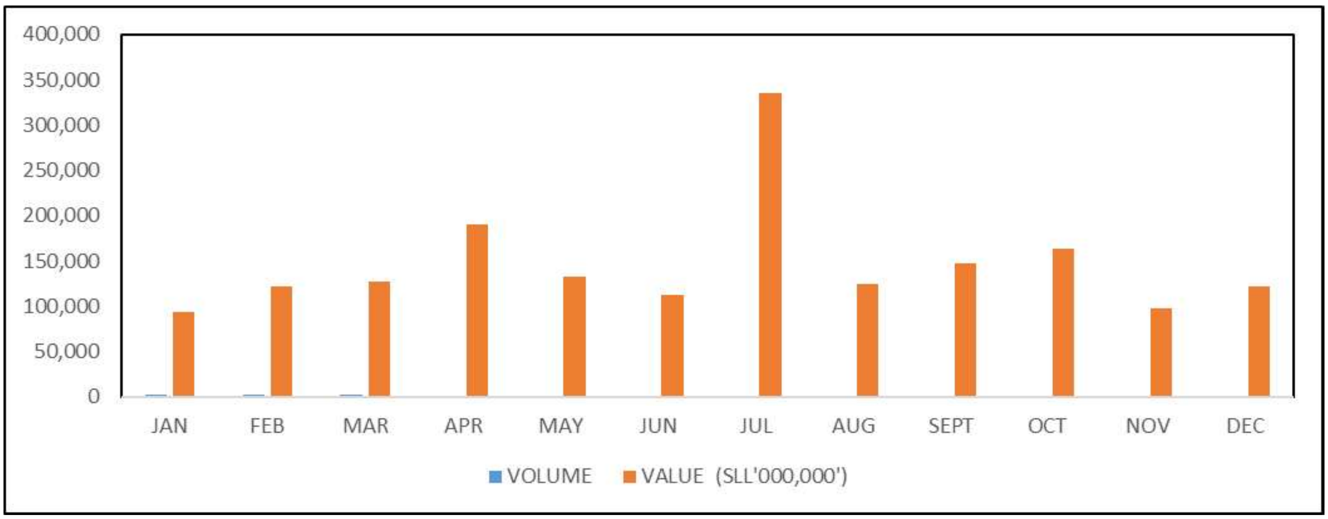
Source: Banking Department, BSL

Figure 6.4: Cheque (SLE) Transactions January-December 2023



Source: Banking Department, BSL

Figure 6.5: Cheque (SLL) Transactions January-December 2023 (Old Currency)



Source: Banking Department, BSL

6.3 Planned Systems and Development

6.3.1 National Payment Switch (NPS)

The NPS is a World Bank funded project which targets establishing interconnectivity and interoperability of all retail payment infrastructures for efficiency in the financial system and help improve rural connectivity. These also include market growth, such as participant connectivity, increased number of value transactions across the switch, increased government payments, increase number of POS terminals, and increase account ownership.

Phase one (1) technically went live on April 29, 2023, with 6 banks. It has since increased to 10 banks. Phase one (1) is the Card Switch, where the NPS interconnects participating banks to allow inter-bank

ATM transactions and inter-bank debit and prepaid card payment in store (POS.). This service becomes important when multiple local banks have deployed automated teller machines (ATMs) and issue debit cards to account holders so that those customers can make balance enquiries, withdraw cash and undertake other banking business at ATMs without visiting a branch.

The next phase will provide an Instant Payment Platform, with the NPS connecting banks and mobile operators together to allow instant payment between customers of different Payment Service Providers (PSP)

The national instant payments platform allows full integration of mobile money with mainstream banking. This platform will enable instant payment from any wallet or bank account, regardless of mobile network. It will also enable instant payment from any current bank account to any account or wallet. This will encourage small businesses to accept payment of goods and services via instant payment and help improve financial inclusion.

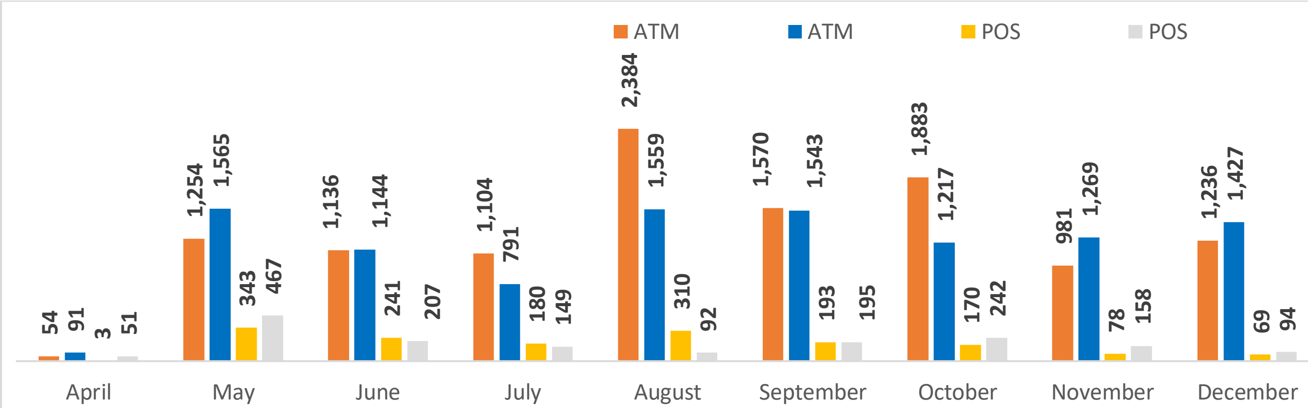
Despite the gains made so far in the payment system landscape, there were still some challenges emanating from Network Connectivity. In most cases this resulted in a lot of failed transactions because of banks network downtime – almost one half of transactions were unsuccessful (*Table 6.1*). Service providers were unable to meet the expected timelines for delivering on the project and the slow adaptation by the commercial banks to participate in the process.

Table 6.1: Summarised SaPS Performance Report 29/04/2023 - 29/12/2023

TRANSACTION SUMMARY	ATM	POS	TOTAL
Successful Transactions (000s)	11.6	1.6	13.2
Unsuccessful Transactions (000s)	10.6	1.6	12.3
SUCCESSFUL VALUE (SLE million)	4.0	2.0	6.0

Source: Banking Department, BSL

Figure 6.6: Summarised Monthly SaPS Transaction Count Performance Report



Source: Banking Department, BSL

6.3.2 AFREXIMBANK – Pan African Payments and Settlement System (PAPSS)

Afreximbank in collaboration with central banks in the WAMZ region are working on a payment and settlement platform to resolve the challenges of cross-border payments in the sub-region. PAPSS has introduced an instant payment solution that will interconnect the national payment systems within the region to promote regional trade.

The BSL is working with PAPSS on this project and are now at the stage of carrying out controlled transactions in the live environment. Also, some commercial banks have been granted no-objection to participate in the PAPSS initiative.

Therefore, given the increase in the acceptability of electronic payment systems in the country, there is a need to improve existing market infrastructures and establish or deepen the payment systems landscape.