

Economic and Budget Brief

Introduction

The Parliamentary Budget Office (PBO) was established in 2017, pursuant to Section 13(1) of the Parliamentary Service Act of 2007, with the aim of maintaining a high quality research, and studies to provide information on economic and financial interests, advise the Legislature on budget matters, and support the legislative process through the costing of proposals initiated by the Executive arm of Government. The above is achieved through the deployment of many processes and procedures such as preparing analysis and briefs relating to the economy and public finances, analysing government budget policies and intentions, and assist in strengthening the work of Parliamentary committees responsible for budget oversight.

This Half-yearly Economic and Budget Brief published by the PBO is intended to update Members of Parliament (MPs) on recent macroeconomic, fiscal and budgetary developments. It utilises published and official data and reports provided by the Ministry of Finance, the Bank of Sierra Leone, Statistics Sierra Leone and where applicable, other institutions. The focus of the analysis is for the period January to June 2020.

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Macroeconomic Developments

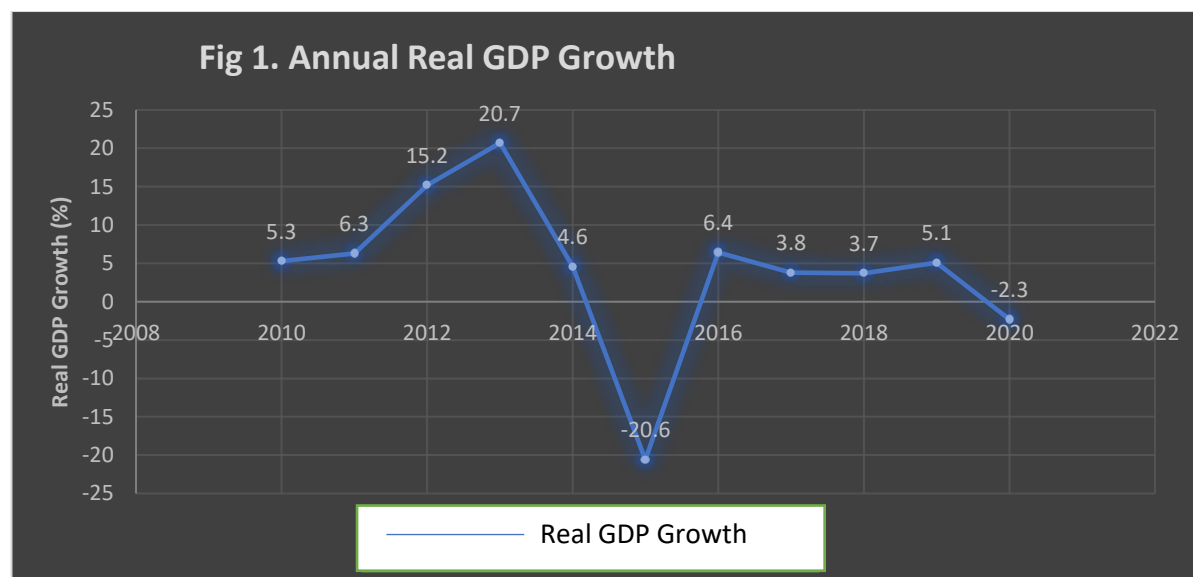
Gross Domestic Product

Global growth is projected at -4.9 percent in 2020, 1.9 percentage points below the April 2020 World Economic Outlook (WEO) forecast. The COVID-19 pandemic has had a more negative impact on activity in the first half of 2020 than anticipated, and the recovery is projected to be more gradual than previously forecast. In 2021 global growth is projected at 5.4 percent. Overall, this would leave 2021 GDP some 6½ percentage points lower than in the pre-COVID-19 projections of January 2020. The adverse impact on low-income households is particularly acute, imperiling the significant progress made in reducing extreme poverty in the world since the 1990s¹.

Sierra Leone Context

The coronavirus pandemic (COVID-19) has reversed the strong growth projections reported earlier in the 2020 IMF Economic Outlook. This has necessitated revisions of the growth projections and outlook for Sierra Leone for 2020 and 2021, accounting for the impact of the COVID-19 pandemic on Sierra Leone's socioeconomic landscape. Uncertainty is heightened by the epidemiology of the virus and the various containment policies adopted by the government. Due to the fluidity of the pandemic, two possible scenarios are considered: the baseline assumes that the virus has a substantial impact but of shorter duration, and the worst-case assumes a virulent impact of the virus over a longer duration with the pandemic continuing beyond the first half of 2020.

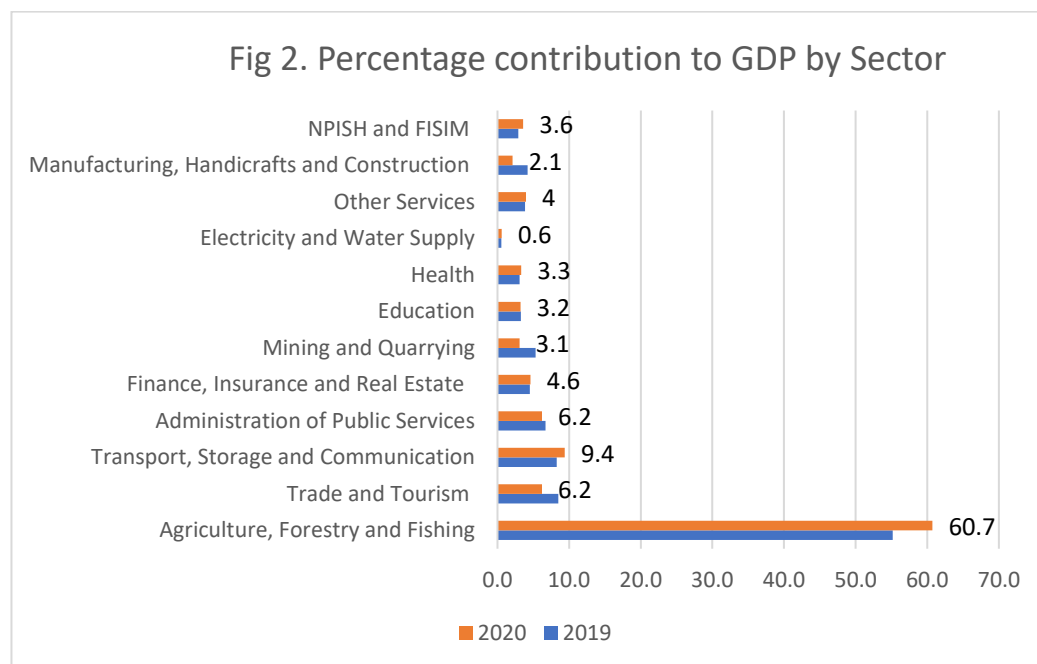
Under the baseline scenario, real GDP is projected to contract by 2.3 percent in 2020, corresponding to a GDP drop of 2.8 percentage points from 2019 annual real GDP growth rate. The country is now faced with the worst-case scenario as the pandemic is set to continue beyond the first half of 2020, as a result we would witness a deeper GDP contraction in 2020.



(Source: PBO calculations based on data published by Statistic Sierra Leone)

¹World Bank Economic outlook report 2020

With the slowdown in performance of the mining sector in Sierra Leone, agriculture continues to be the backbone of the economy with the cultivation of food crops, tree crops, livestock, fisheries and forestry sub sectors accounting for 60.7 percent of GDP in 2020 as compared to 55.2 percent in 2019. The Services sector inclusive of Tourism and Trade, Transport, Finance and Administration of public services decline from 39.8 percent to 39.3 percent and tourism being the most hit sector due to the covid-19 pandemic.



(Source: PBO calculations based on data published by Statistic Sierra Leone)

Inflation Outlook

Based on its assessment, the Bank of Sierra Leone Monetary Policy Committee (MPC) noted that inflationary pressure, after moderating in April 2020 picked up in May 2020, with headline inflation increasing to 15.5% in May 2020 from 15.1% in April 2020. The increase in inflation was mainly driven by food prices, emanating from the impact of COVID-19 related containment measures on the market for essential commodities on the demand side. On the supply side, the restriction on the movement of people and commodities caused a decrease in the supply of essential food stuff from the provinces to Freetown. Both shocks resulted to an increase in inflation rate. The PBO notes that data for June is yet to be published by the Bank of Sierra Leone.

Box1: Contributions to headline annual (YOY) consumer price inflation

✓ Food and non-alcoholic beverages increased from 10.54 percent in April 2020 to 16.60 percent in May 2020. The inflation rate increased by 6.06 percentage points year-on-year.

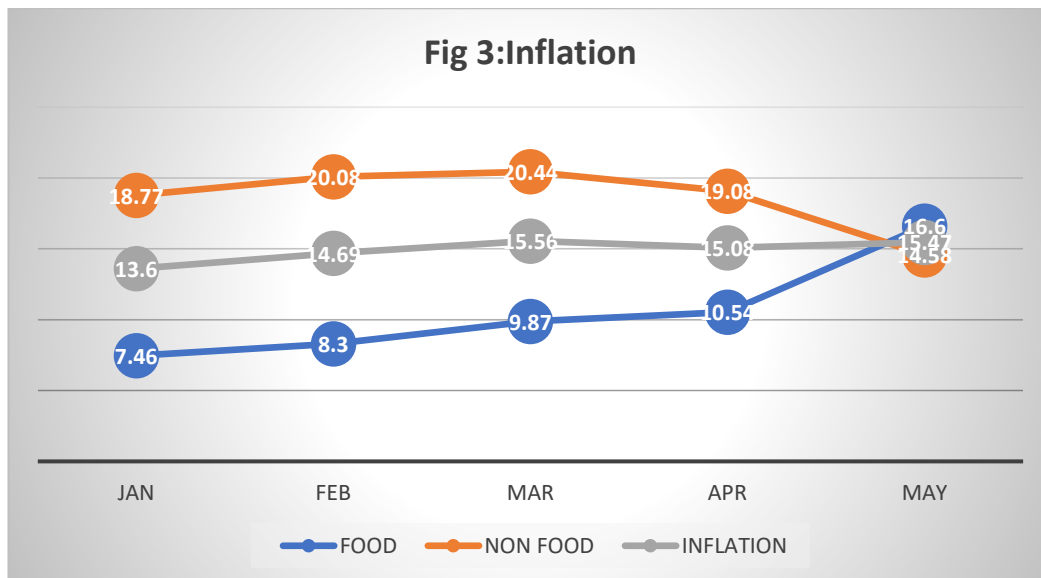
✓ Alcoholic beverages, tobacco and narcotics increased from 1.62 percent in April 2020 to 4.44 percent in May 2020. The inflation rate increased by 2.82 percentage points year-on-year.

✓ Clothing and footwear declined by 2.14 percentage points from 10.43 percent in April 2020 to 8.29 percent in May 2020.

✓ Housing, water, electricity, gas and other fuels increased from 1.98 percent in April 2020 to 5.69 percent in May 2020. The inflation rate increased by 3.71 percentage points year-on-year.

✓ Furniture, household equipment and household maintenance declined by 7.38 percentage points from 7.66 percent in April 2020 to 0.28 percent in May 2020.

✓ Health declined by 18.70 percentage points from 52.31 percent in April 2020 to 33.61 percent in May 2020



Source: PBO calculations based on Statistics Sierra Leone data

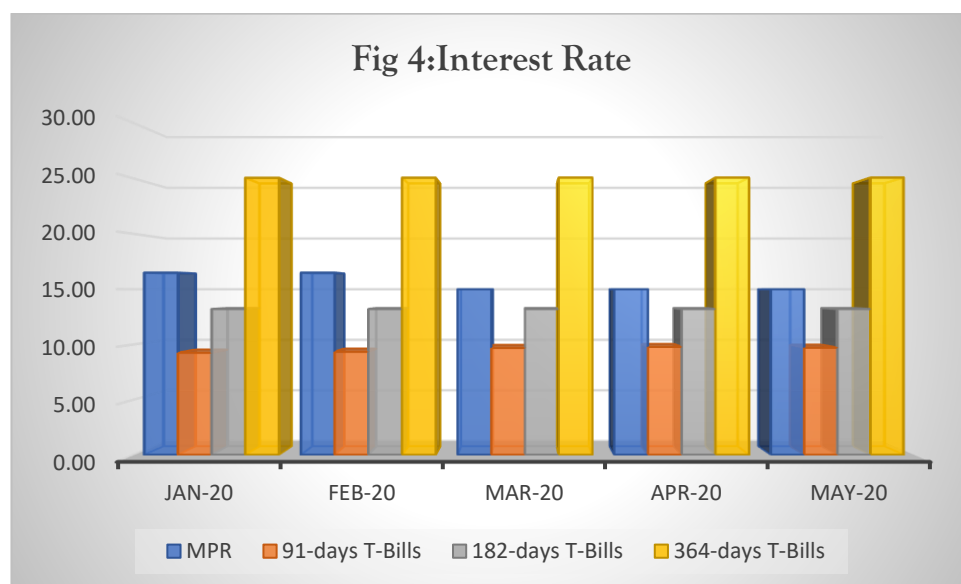
Figure 2 shows a graphical representation of inflation trend in the first half of 2020 for food, non-food and inflation rate.

Food inflation recorded for March increased from 9.9 percent to 10.6 percent in April, and nearly double to 16.6 percent by the end of May. Non-food inflation showed mixed trends between the period Jan to May, rising from 18.8 in Jan and declining to 14.6 in May 2020. The PBO notes that year-on-year consumer price inflation for items in the CPI basket such as housing, water, electricity, gas, fuel and health have continuously fluctuated over the period.

Monetary Policy Rate and Interest Rate

As at Jan 2020, MPC kept the Monetary Policy Rate at 16.5 percent unchanged from Jan to Feb based on the Committee’s analysis of global and domestic macroeconomic performance and the outlook of key macroeconomic indicators, falling to 15.5 percent in Mar until May. Throughout the period Jan to May, the monthly savings rate continued to remain sticky at 2.38 percent, also the average lending rate remained constant at 21.35 throughout the first quarter of 2020. **The PBO notes that high lending interest rates pose a great challenge to businesses which require loans to finance their business undertakings, and it may also lead to unfavorable effects on aggregate demand.**

The interest on government securities showed mixed trends over the period. Between Q1 and Q2, the yield on 91-days treasury bills increased from 9.25 percent to 9.34 percent between Jan and Feb, while the yield on 182-days treasury bills remained constant at 13.21 percent for the first half of 2020. However, the yield on 364-days treasury bills increased marginally from 25.05 percent to 25.07 percent reflecting government’s ongoing appetite to borrow from the domestic market and the high interest rate environment².



Source: PBO calculations based on Bank of Sierra Leone data

²Monthly Economic Review January – May 2020, Bank of Sierra Leone

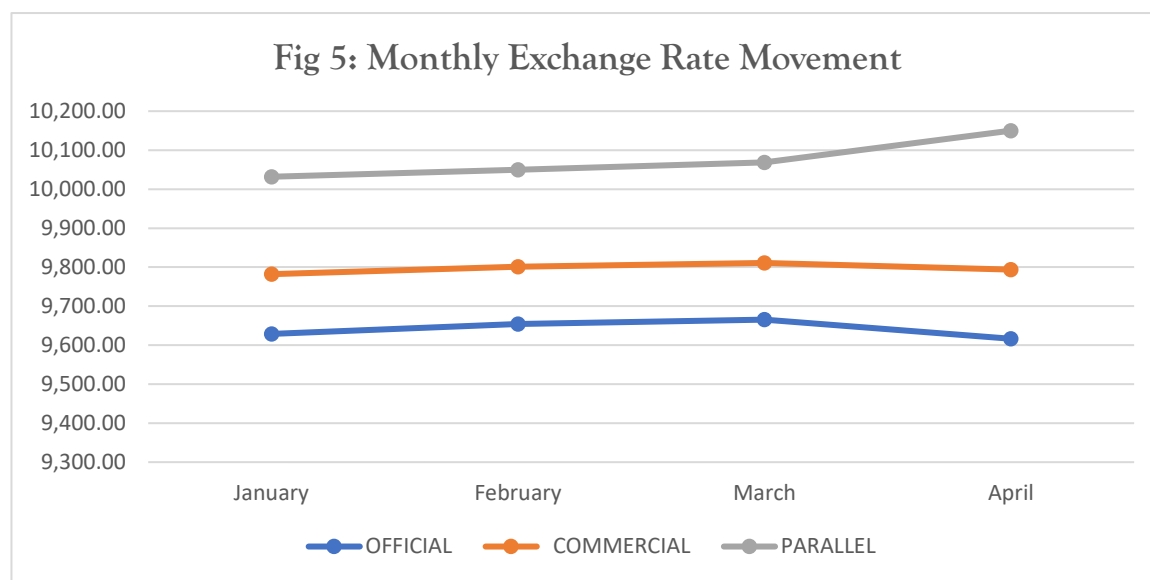
Exchange Rate

Developments in the foreign exchange markets during the first quarter of 2020 month were mixed, the official, commercial and parallel quarterly average of the buying front of the Leone to the US dollar marginally depreciated by 0.15 percent in January, 0.27percent in February, 0.11 percent in March and 0.15 percent in April of 2020 respectively.

The average exchange rate for the first four month of the first quarter shows constant depreciation on all fronts for the Leones against the US dollar. The official monthly exchange rate for January, February, March, and April were as follow Le9,629/US\$1, Le9,655/US\$1, Le9,665/US\$1 and Le 9,617/US\$ 1 respectively.

The average monthly premium between the official and parallel rate widened by 38.1 percent from 338.14/US\$1 in March 2020 to Le 467.10/US\$ 1 in April 2020. The continued upward movement in the exchange rate mirrors the surplus demand for foreign currency which is mainly attributable to the increased demand for imports and unfavorable export performance.

Challenges in the management of the exchange rate include the unwillingness or inability of commercial banks to pay foreign currency account holders in in foreign currency on demand, and the high service charges commercial banks levy for official foreign exchange transactions which gives room for manipulation by the parallel market. The graphical representation gives further insight on the exchange rate performance overtime³.



(Source: PBO calculations based on Bank of Sierra Leone data)

³Monthly Economic Review January – May 2020, Bank of Sierra Leone

Performance by Revenue Heads

Box2: *The fiscal deficit would widen due to the substantial loss in fiscal revenues as external and domestic activity declines and as previously expected revenue administration gains are no longer feasible. Compared to pre-COVID projections, the domestic revenue-to-GDP ratio is expected to drop by 1¾ percentage points, on the back of lower customs duties, value-added tax proceeds and income tax⁴.*

Income Tax: At the beginning of the financial year the performance of income tax was encouraging even though the economy is experiencing a shock since the country recorded its index case of COVID 19. Performance was down when compared with 2019, although there was a significant increase in revenue from Le143, 612 billion in January to Le217, 698 billion (34%) by June from tax collected in the first half of the year.

Goods and Services Tax: According to data published by the ministry of finance goods and services tax raised Le463, 439 billion in the first half of 2020 compared to Le509, 433 billion for the same period in 2019. Performance was sluggish throughout the period, largely affected by COVID 19.

Mineral Resources: The mineral sector continues to perform well despite the pandemic. In the first half of 2020 the mineral sector raised Le123, 880 billion compared to Le117,717 billion in the same period of 2019. Performance from **Fisheries** on the other hand showed a mixed trend, down by just over 2 percentage points for the same period in 2019.

Other Departments which comprise Royalties etc on Fisheries, Parastatals, other revenues (including TSA agencies and Timber) performed poorly as a percentage of contribution to total revenue. As with other revenue streams performance in this area was affected by COVID 19, however its percentage contribution to revenue was 1 percent down on comparison for the same period in 2019. Similarly, there was a decrease in **excise duty on Petroleum Products**. Revenue of Le 171.4 billion was nearly Le 20 billion down when compared with the same period in 2019.

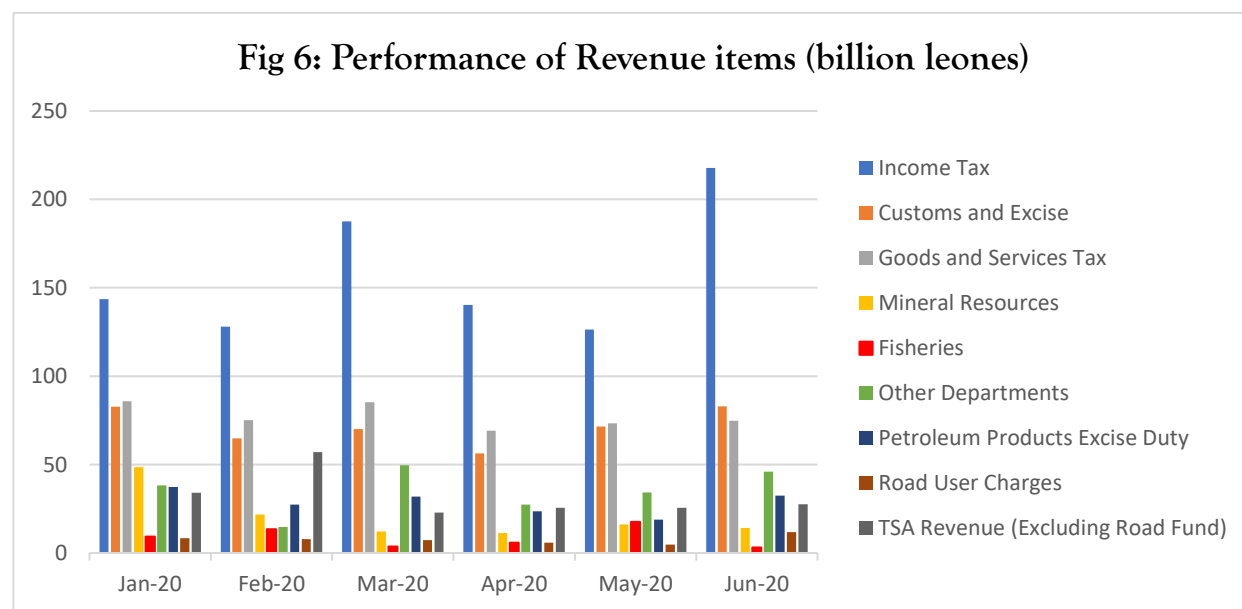
Road User Charges. Revenue generation for this sector fell from Le49, 184 in 2019 to Le45, 923 billion for the same period 2020, reflecting what appears to be the adverse effect of COVID 19 on the economy.

Treasury Single Account. Revenue collected by TSA agencies fell by Le4.4 billion to Le192.9 billion from Le197.3 billion when compared with the same period in 2019.

⁴IMF Country Report 20/196

Table 1: Domestic Revenue Performance (in billion Leones)

Income Tax	143.6	128.0	187.6	140.3	126.4	217.7	943.5	35.8
Customs and Excise	82.8	64.8	70.1	56.4	71.5	83.0	428.6	16.3
Goods and Services Tax	85.8	75.1	85.3	69.1	73.3	74.8	463.4	17.6
Mineral Resources	48.5	21.7	12.2	11.2	16.2	14.1	123.9	4.7
Fisheries	9.2	13.5	3.6	5.8	17.6	3.2	52.8	2.0
Other Departments	38.2	14.7	49.6	27.4	34.2	46.1	210.1	8.0
Petroleum Products Excise Duty	37.4	27.3	31.9	23.5	19.0	32.4	171.4	6.5
Road User Charges	8.4	7.8	7.3	5.8	4.8	11.8	45.9	1.7
TSA Revenue (Excluding Road Fund)	34.1	57.1	22.9	25.5	25.6	27.6	192.9	7.3



Source: PBO calculations based on monthly Fiscal Reports published by the Ministry of Finance

Expenditure Performance

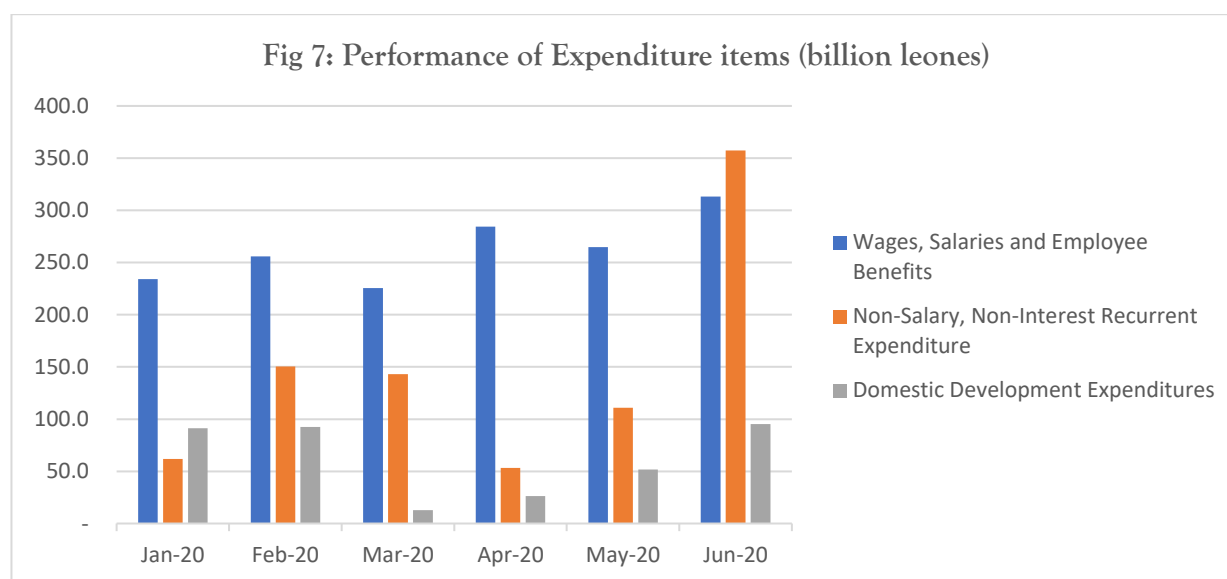
Wages, Salaries and Employee benefit: Spending in wages, salaries, and employee benefit increased by Le371 billion to Le1, 577,608 trillion in the first half of 2020 from Le1, 206,602 trillion for the same period in 2019. New MDAs were created and new staff recruited by the government.

Non-Salary, Non-Interest Recurrent Expenditure: There was a 20 per cent decline in the non-salary, non-interest recurrent expenditure from Le1, 057,797 trillion in 2019 to Le876, 852 billion for the same period in 2020. The inconsistency in spending patterns was especially noted from one month to the next during the period.

Expenditure on Domestic Development contributed 11.2 percent of total operating expenses at Le369.9 billion in the first half of 2020 as compared to Le371.9 billion for the same period in 2019.

Table2: Domestic Expenditure Performance (in billion Leones)

Expenditure	Jan	Feb	Mar	Apr	May	Jun	Total	As a %
Wages, Salaries and Employee Benefits	234.0	256.0	225.5	284.3	264.7	313.1	1577.6	48.3
Non-Salary, Non-Interest Recurrent Expenditure	61.8	150.4	143.2	53.4	110.8	357.3	876.9	26.6
Domestic Development Expenditures	91.2	92.5	12.9	26.3	51.8	95.2	369.9	11.2



Source: PBO calculations based on monthly Fiscal Reports published by the Ministry of Finance

Fiscal Policy to mitigate the impact of COVID-19

The impact of the crisis, and the Government's response, will widen the fiscal deficit. While revenues are set to decline, additional public spending is needed to address immediate health costs, enhance social security, and support the private sector.

- Initial containment measures included ramping up security and provisions for personnel enforcing border closures, screening and so on, and raising public awareness (Le 294 billion).
- Health spending is focused on increased testing and surveillance, laboratory information, case management, information and social mobilization, and logistics. While the health response is still being finalized, the budgetary cost is expected to be around Le 423 billion.
- Mitigating the socio-economic impact. The Government is expanding cash and in-kind transfer programs to vulnerable households in rural areas, and providing one-time payments to affected informal sector workers in urban areas with World Bank support, based on existing structures and in coordination with the Quick Action Economic Response Plan (QAERP) social protection working group. It also plans targeted and temporary import tax deferrals to help secure imports of essential goods. Leveraging already-budgeted projects and existing policy mechanisms, it intends to expand rural road networks and road maintenance in support of employment and private sector activity. These activities require funding of Le 464 billion (around US\$40-45 million).

Notwithstanding efforts to reprioritise 2020 budget spending and scaled-up financing from other development partners, a significant financing gap remains. The total fiscal impact of the COVID-19 related shock, both to revenue and expenditure, is approximately US\$230 million. While the authorities have identified elements of the 2020 budget that will be reallocated to address crisis needs (US\$18.7 million), there will be a substantial fiscal financing gap in excess of Le 2 trillion (around US\$210 million or around 5.4 percent of GDP).

Development partners are moving quickly to commit additional emergency support, significantly narrowing the initial financing gap. The World Bank is providing support for the Health sector response, including a US\$7.5 million health project grant approved in April, and a US\$100 million budget support grant (US\$40 million above the financing provisioned in the authorities' 2020 budget), expected to be approved in June. The European Union is delinking fixed and flexible tranches of their budget support to enable earlier disbursements, and is exploring increased support⁵.

⁵IMF Country Report 20/196

Selected Glossary

Consumer Price Index (CPI) - is a measure of the aggregate price level of a basket of consumer goods and services in an economy.

Exchange Rate - is the value of one nation's currency versus the currency of another nation or economic zone. If it is said that the Leone fell against the US dollar, it means that the Leone is now worth fewer dollars.

Gross Domestic Product (GDP) - is a monetary/standard measure of the market value of all the final goods and services produced by a country during a period. GDP is the single most important indicator to capture economic activity, but it is not necessarily a good measure of societies' wellbeing.

Inflation - is a sustained increase in the general price level of goods and services in an economy over a period of time during which money loses some of its value because its purchasing power falls.

Monetary Policy - refers to how central banks manage liquidity by changing interest rates to control the demand for money and hence the rate of increase of bank lending. This in turn affects the level of demand in the economy and other parameters such as borrowing for consumption and investment.

Monetary Policy Rate - is the rate that is used by the central bank to implement or signal its monetary policy stance, and it is commonly set by the Monetary Policy Committee (MPC).

The **Monetary Policy Committee** consists of seven (7) members as provided for in the **BSL Act, 2011** Section 21(2). They include the Governor, the Deputy Governor, three (3) persons appointed by the Governor and two (2) persons appointed by the Minister of Finance and Economic Development.

Real GDP - is a measure of economic output that accounts for the effects of price changes (i.e. inflation or deflation).

Disclaimer

This Brief has been prepared and published by the Parliamentary Budget Office (PBO) for use by Members of Parliament to enable them to make meaningful contributions on matters around the national budget. The PBO takes full responsibility for its content and may make alterations to the information contained therein at any time.

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