THE GAMBIA

FINANCIAL SECTOR ASSESSMENT

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Prepared By
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A World Bank mission visited The Gambia between February 28 and March 13, 2022, to conduct the Financial Sector Assessment Program (FSAP).[1] This report summarizes the main findings of the mission, identifies key financial sector vulnerabilities, and provides policy recommendations.

[1] The team comprised Carlos Piñerúa (Lead, World Bank), Katie Kibuuka, Pasquale di Benedetta, Ivor Istuk, Holti Banka, Ou Nie (all World Bank), and Engin Akçakoca (expert consultant).

GLOSSARY

ACH	Automated Clearing House	MoJ	Ministry of Justice
B2B	Business-to-Business	MoLRG	Ministry of Lands and Regional Government
CBG	Central Bank of The Gambia	MoTIE	Ministry of Trade, Industry, Regional Integration and Employment
CGS	Credit Guarantee Scheme	MMOs	Mobile Money Operators
CRB	Credit Reference Bureau	MNOs	Mobile Network Operators
CUs	Credit Unions	MTOs	Money Transfer Operators
DGA	Deposit Guarantee Authority	PEC	National Assembly Public Enterprise Committee
FCs	Deposit Taking Finance Companies	NACCUG	National Association of Cooperative Credit Unions of The Gambia
DFS	Digital Financial Services	NAO	National Audit Office
EWS	Early Warning System	NAWEC	National Water and Electricity Company
ECOWAS	Economic Community of West African State	NFES	National Financial Education Strategy
ELA	Emergency Liquidity Assistance	NFIS	National Financial Inclusion Strategy
ERM	Enterprise Risk Management	NPF	National Provident Fund
FPS	Federated Pension Scheme	NBFIs	Non-Bank Financial Institutions
FSC	Financial Stability Council	NPLs	Non-Peforming Loans
FSU	Financial Stability Unit	OFI	Other Financial Institutions
FSD	Financial Supervision Department	PCG	Partial Credit Guarantee
FSSR	Financial Sector Stability Review	PayTech	Payment Technology
FinTech	Financial Technology	PS	Permanent Secretary
FX	Foreign Exchange	POS	Point-Of-Service
GMD	Gambia Dalasi	RTGS	Real Time Gross Settlement
GIEPA	Gambia Investment and Export Promotion Agency	ROA	Return on Assets
GAMSwitch	Gambia National Card Switch	ROE	Return on Equity
GhIPSS	Ghana Interbank Payment and	SSS	Securities Settlement System
GRA	Gambia Revenue Authority	SMEs	Small and Medium Enterprises
G2B	Government-to-Business	SDF	Social Development Fund
HFF	Housing Finance Fund	SSHFC	Social Security and Housing Finance Corporation
IICF	Industrial Injuries Compensation	SOE	State-Owned Enterprise
KPIs	Key Performance Indicators	SSA	Sub-Saharan Africa
KYC	Know-Your-Customer	UBOs	Ultimate Beneficial Owners
LICs	Low Income Countries	UNCDF	United Nations Capital Development Fund
MD	Managing Director	VISACAs	Village Savings and Credit Associations
MSMEs	Micro, Small and Medium Enterprises	WAMZ	West African Monetary Zone
MoBSE	Ministry of Basic and Secondary Education	WEF	Women's Enterprise Fund
MoFEA	Ministry of Finance and Economic Affairs	YEP	Youth Empowerment Project

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PREFACE

A World Bank team visited Gambia between February 28 and March 13, 2022, to conduct an assessment under the Financial Sector Assessment Program (FSAP): Development Module. This is the first FSAP conducted in The Gambia. The team was led by Carlos Piñerúa, and included Katie Kibuuka, Pasquale di Benedetta, Ivor Istuk, Holti Banka, Ou Nie, and Engin Akçakoca. The mission assessed financial sector risks to, constraints to, and opportunities for financial sector development in the Gambia.

The mission met with Mr. Buah Saidy, the Governor of the Central Bank of the Gambia (CBG); Dr. Seeku Jaabi, First Deputy Governor CBG; Mr. Essa Drammeh, Second Deputy Governor CBG; directors and other senior staff from the CBG. On behalf of Hon. Mambury Njie (Minister of Finance), the team met with Mr. Baboucarr Jobe, Director of Economic Policy & Research, Ministry of Finance and Economic Affairs (MoFEA); and the Directorates of Loans and Debt Management, State Owned Enterprises, and Public Private Partnership (MoFEA). The mission also met with Mssrs. Buba Sanyang and Muntaga Sallah, the Permanent Secretaries of the Ministry of Lands and Regional Government (MoLRG); and other senior staff from the MoLRG. Lastly, the mission met with Mr. Abdoulie Tambedou, the Managing Director of the Social Security and Housing Finance Corporation (SSHFC); directors and senior staff from SSHFC.

The mission wishes to extend its appreciation to the Gambian authorities, Gambian Commercial Banks, Finance companies, credit unions, and other representatives from the private sector for their cooperation and constructive discussions. In addition, the mission offers special thanks to Ms. Halima Singhateh, Deputy Director – Department of Financial Supervision (CBG), Mr. Siaka Bah, Director - Other Financial Institutions (CBG), and Ms. Yamundow Sey from the Directorate of Macroeconomic Policy Analysis (MoFEA) for facilitating the work of the mission. The mission would also like to thank Ms. Yassin Saine Njie (World Bank country office) for her valuable logistical support and assistance.

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EXECUTIVE SUMMARY

The Gambia is a small and fragile country that is struggling with significant development challenges and has reached a critical juncture in its growth trajectory. In 2020, the country had a population of about 2.4 million and a GDP of about USD 1.9 billion. The economy relies heavily on rain-fed agriculture and seasonal tourism while a unique country context, largely driven by structural deficiencies and a legacy of institutional fragility, contributes to a volatile and uneven growth path. Real GDP growth averaged 3.5 percent (less than 0.5 percent in per capita terms) between 2000 and 2018, lower than the Sub-Saharan African average of 4.6 percent. As a result, almost half the population was estimated to be living in absolute poverty. Despite multiple setbacks since political transition in 2016-17 (in particular, the onset of the COVID-19 pandemic), the current administration has made headway on key reforms and service delivery, laying the foundation for a new development path. With the impact of the pandemic fading and the recent validation in democratic processes, there is an opportunity to accelerate reforms needed to engineer structural transformation and to shift the economy onto a more sustainable and inclusive growth path.

A stable and inclusive financial sector is crucial to achieving Gambia's economic transformation, however the current system is unable to play the role of an effective enabler of the private sector. The financial sector is small, bank dominated, and characterized by low financial intermediation. Access to credit, particularly by smaller enterprises, remains limited, undermined by structural and regulatory deficiencies. Similarly, most of the population remains underserved by the sector. The banking sector, which is mostly foreign owned, requires a balanced approach to regulatory and supervisory efforts to address vulnerabilities, to instill confidence and to maintain resilience. Meanwhile, other financial institutions are small and have yet to offer financial services and products that are attractive to Gambians. Digital payments and other digital financial services (DFS) remain underdeveloped compared to peer countries. Longer term financial institutions, including capital markets, do not yet represent a potential alternative avenue for financing. Lastly, the sector is dominated by a state-owned entity which, for too long, has represented a key vulnerability for stability and market development. Many of these challenges have been exacerbated by the pandemic, which has brought added urgency to implementing policy actions to address them.

The banking sector is rather well-funded and is relatively large based on asset size, but it struggles to allocate these resources to the private sector, resulting in low financial intermediation indicators. Gambian bank funding, measured by bank deposits to GDP, compared well to peer comparison groups, at about 50 percent at end-2021 and about 45 percent at end-2020, higher than the Sub-Saharan Africa (SSA) regional median of 27 percent and the SSA Low Income

Countries (LICs) average of 26.5 percent. In addition, the size of the banking sector, measured by total banking sector assets to GDP, was relatively larger than peer comparators. At end-2021, banking sector assets were 70.5 percent of GDP, much larger than the SSA region median of 53 percent of GDP while the SSA LICs average of 47.2 percent of GDP. Despite these attributes, the Gambian banking sector has great difficulty in allocating these resources to the real sector and, in turn, fuel private investment. This is illustrated by significantly low financial intermediation indicators compared with peers. Notedly, bank credit to GDP stood at about 9 percent at end-2021, significantly lower than the SSA median of 14.9 percent and the SSA LICs average of 14.6 percent. In addition, the loan to deposit ratio at 17.5 percent in 2021, is far below the SSA median of 67 percent and the SSA LICs average of 70.8 percent.

Challenges faced by the banking sector in supporting the private sector are further aggravated by vulnerabilities and risks that increased during the pandemic. The halt in economic activity at the onset of the pandemic affected borrowers' ability to meet their financial obligations with financial institutions. Meanwhile, uncertainty increased during this period which raised the risk aversion of financial service providers, reducing their willingness to lend as well as innovate. Building on the IMF Financial Sector Stability Review (FSSR) conducted in November 2019, this assessment finds that the main sources of vulnerabilities and risks were linked to deteriorating asset quality (or increasing non-performing loans – NPLs), funding concentration risks, declining profitability, and longstanding structural issues. In addition, supervisory forbearance measures, designed to support the sector during the pandemic, may have increased risks, particularly by weakening bank provisioning – which is designed to support bank resiliency as NPLs increase. Enhanced monitoring of banks with portfolios at risk (high NPLs) and/or subjected to forbearance measures) is required to ensure bank soundness. Remedial actions should be governed by a full stocktaking of financial sector stress (especially small banks and non-bank financial institutions - NBFIs) resulting from the withdrawal of forbearance measures and further monitoring of the lagged effects of the pandemic.

Declining profitability and funding concentration risks are of particular concern for small banks and need to be mitigated by withdrawing the lending rate guidance while enhancing the monitoring and regulation of large deposit exposures. Mostly negative rates in real terms on government securities reduced earnings from the bulk of banks' assets. Difficulties in shifting bank business models in the medium term and heavy competition for very few creditworthy firms have affected profitability. These conditions are exacerbated by a lending rate guidance that sets a maximum lending rate of 15 percent. This rate ceiling does not sufficiently cover costs for banks with high average funding costs or high overhead costs related to dealing with riskier clientele. In fact, banks have reduced lending given this guidance, curtailing most lending to riskier market segments, such as agriculture as well as medium and small enterprises (MSMEs). This guidance not only further compounding issues of low intermediation and inclusion, but it limits options that development partners can initiate to support financial sector development in the Gambia. Meanwhile high concentrations of deposits from the Social Security and Housing Finance Corporation (SSHFC), the largest institutional investor in the financial sector, in funding portfolios pose systemic risks. Small banks are the most vulnerable to these issues.

Weaknesses in the current bank regulatory and supervisory framework affect the Central Bank's ability to effectively address vulnerabilities and risks, and to proactively safeguard the banking sector. Again, building on the IMF FSSR, the assessment highlights a number of regulatory and supervisory issues that need to be promptly addressed to ensure that, in the short term, the Central of Gambia (CBG) is well-prepared and has the authority to restore banking sector soundness. These issues include, amongst others: i) challenges to the Central Bank of Gambia (CBG) independence; ii) no description of ultimate beneficial owners (UBOs); iii) lack of clarity on corrective measures and triggers for intervention; iv) weak risk management and corporate governance systems; v) the lack of a formal resolution framework; vi) undefined power and unclear enforceability of secondary legislation; vii) lack of emergency liquidity assistance (ELA) regulation; and viii) lack of a contingency planning framework in banks' liquidity risk management policies. In the medium term, these actions help to build confidence in the banking sector, which is a cornerstone to increasing and broadening usage of financial services.

As the banking sector is predominantly foreign owned, efforts to strengthen cross border supervision and resolution are particularly critical to ensuring sector stability and confidence. Currently, the CBG relies on the West African Monetary Zone (WAMZ) supervisory college to conduct cross-border supervision and to facilitate cross-border cooperation for supervising the parents of foreign banks in the system. While this arrangement has not created major issues so far, it will likely prove inefficient during a rapid-response situation to address an urgent bank issue according to international standards. As such, the CBG should start working directly with supervisors of parent banks to develop specific action plans aiming at resolving parent/subsidiary weaknesses. In addition, there is no framework in place to facilitate cooperation in cross-border resolutions. Although, the College of Supervisors of WAMZ is working on a draft bank resolution framework, the Gambian Banking Act should be amended to give a wider range of cooperation and exchange of information powers to the CBG with home supervisors and resolution authorities, including sharing recovery and resolution plans of the banking institutions and their parents. It is also important that the CBG work with parent banks' supervisors and resolution authorities in the preparation of contingency resolution plans.

In addition to increasing stability, expanding financial sector inclusiveness is essential to achieving the Gambia's development plans, especially ensuring MSME access to credit. The bulk of the private sector in the Gambia is comprised of MSMEs. Unleashing private sector-led growth will require increased investment in these entities. As noted earlier, bank financial intermediation is very low. As a result, only 10 percent of small and 12 percent of medium-size firms have access to (bank) credit, which compares poorly to the Sub-Saharan Africa region ratios of 16 percent and 26 percent, respectively. Banks are focused on serving the public sector and corporates, limiting MSME access to their financial services. Consequently, MSMEs tend to access formal financial services mostly from non-bank financial institutions (NBFIs), which often lack the capacity to lend (specifically providing longer tenor funding) and the propensity to innovate (capacity to adequately serve their clientele). NBFIs are also excluded from important segments of the financial infrastructure, effectively discarding valuable financial information. Fintech has not substantially penetrated the market yet, mostly due to the lack of regulatory clarity.

Structural challenges have persistently hindered financial intermediation in the Gambia, disproportionately affecting MSMEs. All financial institutions cite financial information asymmetries and weak contract enforcement as well as foreclosure issues as significant obstacles to their ability to intermediate more funds. Quick wins are possible by improving the quality of credit reporting data while expanding coverage to the NBFI sector to help reduce information asymmetries. Secondly, weak enforcement of creditors' rights is mainly due to a fragmented legal framework, lengthy court proceedings, and difficulties in enforcing judgements, which all undermine NPL resolution. This, in turn, raises the risk aversion of financial institutions which translates into higher risk premia and higher costs of credit for riskier borrowers like MSMEs. Efforts to re-establish specialized commercial courts, including reviewing the legal framework for contract enforcement and strengthening judicial capacity, are a good start to addressing these issues in the short to medium term. On the demand side—factors that increase the perception of risk and enhance information asymmetries—challenges include a high level of informality in the economy, a lack of financial management and financial reporting by MSMEs, and the dominance of cash as a preferred mean of payment, which makes it difficult to leverage the potential of digitizing access to finance. Reform priorities should include efforts to improve firm capabilities and bankability through business development services and financial education for entrepreneurs. In addition, the NBFI regulatory framework needs to introduce risk-based regulation and to create an environment that is supportive of innovative financial firms (or FinTechs).

Another vital step to increasing financial inclusion is tackling extremely low levels of access to formal financial services caused by a set of multifaceted factors. According to the 2019 FinScope survey, only 19 percent of Gambian adults are formally served by the financial sector while almost 70 percent of Gambian adults are financially excluded. This is much lower than comparison peer countries such as Togo, Benin and Burkina Faso, which report 45, 43, and 40 percent of adults with access to formal financial services, respectively, as well as the LICs average (35 percent) and SSA region average (43 percent). Low financial inclusion is driven by low income, low trust in financial institutions, lack of necessary basic documentation, high fees, and long distances to financial institution branches. While low incomes are the result of the country's fragility and low economic growth, factors such as low trust are associated with lack of financial literacy and "fear" factors[2] that individuals have in using financial services. High costs for financial services point to limited competition as well as a fee-driven model for payment services. Lastly, the lack of necessary documentation to open a transaction account points to the need for a simplified and tiered approach to due diligence procedures, as well as the need to introduce a "basic" bank account product that better caters to many unbanked Gambians.

Increasing access to and usage of transaction accounts has the potential to offer significant financial inclusion benefits while paving the way to a much-needed digital economy. Research has shown many potential development benefits from financial inclusion, especially from the use of digital financial services, including basic transactional accounts like mobile money services or payment cards. Digital financial inclusion promotes efficient interconnection among participants in economic activities. Shifting cash into digital accounts for government payments, remittances, micro, small and medium enterprise (MSME) payments, and agricultural value-chain payments can enable broad-based participation in digital economy. In the Gambia, low access to transaction accounts has also contributed to a low usage of digital payments. Cash and cheques are the predominant payment instruments in The Gambia, while the use of digital payment instruments is limited. According to FinScope, only 5 percent of adults use banking related products (including digital payment instruments) and only 2 percent of the adults use mobile money. Low digital payment usage can be traced back to legal/regulatory gaps and uncertainty, high fees, lack of modernization in underlying payment systems infrastructure, and lack of interoperability between digital payment instruments and access channels. As such, priority action is needed to: i) update the payment systems Act (2016) and the mobile money regulation (2011); ii) increase the role of NBFIs and other excluded actors in the digital payments ecosystem; and iii) upgrade the payment systems infrastructure.

The launch of the National Financial Inclusion Strategy (NFIS) in January 2022 is a welcome development to achieve national financial inclusion goals. The NFIS identifies strategic enablers

[2] For example, perception of lack of soundproof of payment if paper is not used; fear that the new modalities may be vulnerable to fraud; fear of dealing with unresponsive, complicated systems prone to operational error; and perception of loss of privacy

and pillars and puts forward ambitious targets to be achieved by 2025 in addition to allocating responsibilities across different stakeholders in the public and private sector. The Strategy identifies demand side drive, supply side drive and regulatory driven bottlenecks to financial inclusion in the Gambia and includes a series of recommendations on how to address those bottlenecks. International experience indicates that implementation is more effective if the responsible taskforce is converted into a formal body such as a National Financial Inclusion Committee or a National Payments Committee with a mandate beyond the expiration of the current NFIS. This formal entity should have the oversight powers to ensure that critical elements needed to progress and monitor implementation are in place, notedly: i) adequate institutional strength and capacity; ii) high-level political commitment; and iii) close coordination and cooperation with various relevant stakeholders (both private and public).

Though significantly underdeveloped in the Gambia, long-term financial institutions are essential for improving financial depth, diversity, and, ultimately, inclusion. As of 2021, pensions assets accounted for 6 percent of total financial assets (5 percent of GDP), much lower than the SSA region average of 11 percent of GDP. In addition, the main pension scheme administered by the SSHFC has been significantly weakened over recent years and there is no pension regulator. The insurance sector in the Gambia only represents 1.3 percent of total financial sector assets (1 percent of GDP), much lower than the SSA region average of 18.3 percent of GDP. This sector faces many challenges and it is regulated by the CBG, which lacks the specialized personnel to support growth and innovation. At present, there is no capital market, however draft legislation has been submitted to Parliament to establish one.[3] This assessment highly recommends that authorities focus on putting the pre-conditions for capital market development[4] in place to improve the success potential of a capital market. Lastly, the government debt market is characterized by a small and underdeveloped primary market, narrow and undiversified investor base, no liability management operations, and no secondary market trading. A benchmark building strategy can help to prioritize and sequence policy actions needed to support government debt market development.

The Social Security and Housing Finance Corporation (SSHFC) plays an important role in developing longer-term financial markets, but its interconnectedness with other financial institutions and the government can pose a serious risk given its need for a major restructure. The SSHFC manages assets amounting to 7 percent of total financial sector assets (6 percent of GDP). More than half of these assets are placed in government securities and term deposits in commercial

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[3] The mission team did not have an opportunity to review the draft legislation to establish a capital market.
[4] Capital Markets Development: Causes, Effects, and Sequencing, World Bank, December 2019

banks, which can pose systemic risks in some banks. As a key holder of government securities, the sovereign-corporate nexus could amplify negative shocks in times of stress if the government's perceived implicit guarantee of the SSHFC comes into question. The corporation also has substantial shareholding in two banks, including the second largest bank. Meanwhile, independent financial analyses show that the viability of the country's social security system is at serious risk unless structural issues are addressed. The legacy of the past administration has deeply scarred the integrity of the corporation's governance. To achieve the fundamental changes that the current administration desires, several issues will have to be urgently addressed, including: i) the lack of an appropriate corporate governance framework, especially defined fit-and-proper criteria for naming board and management members; ii) unclear and overlapping roles of the Government, the board, and the management which ultimately blur accountability; iii) a lack of reporting discipline and the absence of formal performance contracts with the government to ensure accountability and to track progress; iv) no proper internal control functions (audit, compliance and controls); and v) the absence of Board Audit and Risk Committees.

This assessment welcomes the approved action plan to reform the SSHFC and provides recommendations to ensure its effective implementation. The SSHFC Board approved a strategy (2022-2026) based on a comprehensive five-year restructuring plan to reform operations, processes, controls, and governance. The SSHFC should focus on three main goals to ensure the effective implementation of this plan: i) adequate segregation of duties and functions throughout the institution, particularly the banking and pensions functions; ii) related to business operations, increased ownership over the investment policy currently in draft, which clarifies investment objectives and business targets in addition to developing a dedicated and independent risk oversight function; and iii) strengthening disclosure practices. Internal controls, including audit risk and compliance, will have to be re-designed, made independent, and well-resourced. An Enterprise Risk Management (ERM) framework will have to be designed, implemented, and appropriately resourced. External communication via disclosure of financial information should be re-activated to improve transparency and oversight of SSHFC operations. This information is also important to better understanding the risks that the SSHFC poses in the sovereign-corporate nexus, which warrants further attention, analysis, and action. A newly drafted State-Owned Enterprise (SOE) bill awaits parliamentary approval and addresses some gaps in the legal framework need to improve governance practices within SSHFC. If adequately designed, performance contracts can bring order and clarity to targets, key performance indicators (KPIs), and the overall strategic direction.

Table 1: Gambia FSAP Development Module: Key Recommendations			
Recommendations and Authority Responsible for Implementation	**Agency**	**Time[1]**	**Priority[1]**
Overarching			
Withdraw lending rate guidance	CBG	I	H
Incorporate NBFIs sector into credit reporting and payments infrastructure	CBG	NT	H
Expedite efforts to re-establish specialized commercial courts, including reviewing the legal framework for contract enforcement and strengthening judicial capacity	CBG, MoFEA, MoJ	MT	H
Banking Sector Resiliency			
Initiate phase out of supervisory forbearance measures	CBG	I	H
Enhanced periodic monitoring of banks with portfolios at risk (high NPLs and/or subjected to forbearance measures)	CBG	I	H
Closer monitoring, assessment, and regulation of deposit concentrations	CBG	NT	H
Develop a framework for cross-border resolution, and prepare contingency resolution plans with home supervisors and resolution authorities of parent banks	CBG	NT	H
Access to Finance for MSMEs and Financial Inclusion			
Strengthen credit reporting by enforcing data quality requirements	CBG	I	H
Introduce a simplified due diligence approach and basic bank accounts	CBG	NT	H
Revise the NBFI legal and regulatory framework to introduce risk-based regulation and to create an environment supportive of innovation	CBG	NT	H
Payment Systems and Developing Digital Payments			
Update the Payment Systems Act (2016) and Mobile Money regulation (2011) to include emerging business models and FinTech	CBG	NT	H
Upgrade the RTGS and ACH payment systems infrastructure	CBG	NT	H
Role of the State in developing Long Term Financial Institutions			
Submit the SOE Bill to the National Assembly and revise the SSHFC Act	MoFEA,	NT	H
Sign Performance Contracts with SSHFC	SSHFC, MoFEA, MoLRG	NT	H
Design an Enterprise Risk Management Framework; Secure separation and segregation of pension and banking functions.	SSHFC	NT	H

[1] I-Immediate" is within one year; "NT-near-term" is 1–3 years; "MT-medium-term" is 3–5 years. Priority: H-High; M-Medium; L-Low

I. INTRODUCTION

1. **The Gambia is a small and fragile country that has been struggling with low and volatile growth over the last two decades.** As of 2020, The Gambia had a population of about 2.4 million and a GDP totaling about USD 1.9 billion. The economy is highly dependent on rain-fed agriculture and seasonal tourism, which are highly susceptible to external shocks. In addition, the country suffers from inadequate product and export diversification as well as a weak infrastructure assets and poor service delivery. Authoritarian rule lasting over two decades left the Gambia in a dire economic situation as institutional fragility contributed to the build-up of severe macroeconomic imbalances, high public debt, and a broken social contract among citizens, the state, and the private sector. Real GDP growth averaged 3.5 percent (less than 0.5 percent in per capita terms) between 2000 and 2018, lower than the Sub-Saharan African average of 4.6 percent. Moreover, this period was characterized by high growth volatility and very limited impact on headcount poverty. As a result, almost half the population was estimated to be living in absolute poverty.[5]

2. **A unique country context underlies the country's growth and poverty experience while continuing to pose a significant development challenge.**[6] The interplay of several key factors creates this unique context: (i) persistent fragility, largely driven by a legacy of weak and poor governance; (ii) small state features, which, inter alia, pose significant challenges to development; (iii) deep challenges with low productivity; (iv) unmanaged migration given limited employment opportunities and inadequate human capital investment; (v) rapid urbanization and climate change resulting in land pressures and environmental degradation; and (vi) an unusual geography — the country is almost an enclave in the Republic of Senegal — affecting social and economic integration. The country context is further complicated by stalled political reform and a slow reconciliation process, which has intensified political instability and social tensions.

3. **Following the political transition in 2016-17, the Gambia experienced broad economic rebound consolidated by better economic management and the introduction of a comprehensive reform policy agenda.** Economic growth accelerated from 2 percent in 2016 to 6 percent in 2019.[7] Also, the overall macroeconomic environment improved during this period, namely: i) a broadly stable exchange rate and inflation rate (between 8 and 6 percent); ii) improved debt

[5] The 2015 national household survey reported that 48.6 percent of the population were living below the national poverty line. A new household survey was conducted in 2020/21, but the poverty numbers are yet to be finalized.
[6] World Bank Group, Country Partnership Framework for the Republic of the Gambia for the period of FY22-FY26, March 2022.
[7] IMF World Economic Outlook, April 2022

sustainability prospects given determined fiscal consolidation efforts, and iii) markedly improved official reserves as import coverage increased from about 1 month to 4 months. Tourism rebounded – reaching peak levels of over 200,000 tourist arrivals while business confidence returned causing a rapid expansion in credit to the private sector. Lastly, structural and legislative reforms were advanced across multiple sectors and many social indicators improved, notably those on health and education.

4. **The COVID-19 pandemic disrupted the country's economic resurgence in 2020, impacting hard-won economic gains and amplifying socio-economic fragility.**[8] In 2020, real GDP per capita contracted by 2.7 percent, contributing to an increase in the poverty rate from 8.4 percent in 2019 to 9.2 percent in 2020. An additional 25,000 individuals (nearly 1 percent of the population) were pushed into extreme poverty. 48 percent of businesses reported a partial loss of income, 43 percent scaled back their operations, and 19 percent were shuttered.[9] The worst hit sector was tourism, following travel restrictions that halted global travel – tourist arrivals precipitously declined from 235,710 in 2019 to 89,233 in 2020. Labor market activities were disrupted resulting in a large reduction in employment, especially at the onset of the pandemic. Private consumption contracted by 1.2 percent as almost every household reported a loss of income in 2020, and almost a quarter reported job losses. Despite mitigating measures taken by the government and development partners, the pandemic impacted gains made in human capital accumulation.

5. **With the impact of the pandemic receding, efforts to accelerate structural transformation are required to shift the economy onto a more sustainable and inclusive growth path.** The continued dependence on rain-fed agriculture, inadequate economic diversification, and persistently low productivity levels are symptomatic of limited structural transformation over the last several decades. Sustained government commitment to a comprehensive reform agenda as well as critical human capital and infrastructure investments are required to kickstart the process of structural transformation. Growth and job-creation, especially the creation of quality jobs, will be contingent on the commercialization of agriculture and stimulating expansion of the non-farm sector.

6. **A stable, inclusive financial sector will be critical to Gambia's economic transformation.** Recent improvements in economic conditions open a window for the authorities to take necessary actions to position the financial sector as an effective enabler of the real sector. A significant part of this repositioning will involve a stocktaking of the stress on the financial sector (especially small banks and non-bank financial institutions - NBFIs) resulting from the withdrawal of Central Bank COVID-19 forbearance measures, monitoring the lagged effects of the pandemic, and taking prompt remedial

[8] World Bank Gambia Economic Update, June 2022
[9] IMF Article IV, December 2021

actions to restore soundness. It will also involve facilitating new financial actors and instruments that are better tailored to the demands of the Gambian real sector. Over the longer term, diversified forms of finance will be needed to support the economy, particularly through the development of long-term financial institutions and a capital market.

7. **The areas of focus for this FSAP Development Module are accordingly aligned with priority reforms that can catalyze the supply of finance to the real sector given the current context in Gambia.** Following the descriptive sections, this report takes stock of the vulnerabilities and risks that have accumulated in the banking sector given the impact of the pandemic, then it makes recommendations to manage these risks while shoring up the oversight of current and emerging issues. The next section delves into opportunities to mobilize credit to medium and small enterprises (MSMEs), through alternate institutions and instruments, and critical initiatives to increase financial inclusion. The third section examines the country's payments infrastructure and digital payments landscape, then provides recommendations to strengthen payment systems as well as to expand the usage of digital payments. The last section covers long-term financial institutions which could, in time, provide a more diversified source of domestic capital to support investment in the corporate and real sectors. This section provides an overview of relevant institutions, an assessment of the potential for capital markets development, and the role of the state in developing long-term financial institutions, especially strengthening the Social Security and Housing Finance Corporation (SSHFC).

II. BACKGROUND

A. Macro-financial Context

1. **The Gambia is enjoying a strong recovery from the COVID-19 impact.[10]** Real GDP growth is estimated to have rebounded to 4.3 percent in 2021, or 1.3 percent per capita. Tourism began to recover with arrivals reaching 102,460, a 14.8 percent increase over 2020 arrivals. Favorable weather and timely supplies of inputs enabled strong growth in agriculture. Formal remittances reached a record high of US$777 million (38 percent of GDP), a 31.7 percent increase over 2020,[11] supporting private consumption and investment, particularly in construction. Domestic demand recovery was

[10] World Bank Gambia Economic Update, June 2022

[11] It should be noted that total international remittances to Gambia declined during 2020, however remittances transferred through formal channels increased substantially as COVID-19 movement restrictions affected informal remittance channels and money transfer operators increased. See World Bank Gambia Economic Update, June 2022.

further fueled by rapidly implemented public investment projects. Total public debt to GDP declined to an estimated 83.8 percent of GDP by end-2021. Increased financial flows offset the current account deficit, boosting reserves to 6 months of import coverage. The nominal exchange rate remained broadly stable, but the real exchange rate appreciated slightly. Although volatile (reaching a low of 4.,8 percent in July 2020 and a peak of 8.2 in July 2021), the inflation rate also remained rather steady. Business confidence returned and private sector credit growth grew by 26.5 percent. Following a peaceful election in December 2021, business activity was driven by higher-than-expected sales and resilient profitability in Q1 2022.

2. The somewhat positive economic outlook faces headwinds from high uncertainty. The Gambia's strong recovery is expected to continue, albeit modestly, spurred by increased tourism activity, a rebound in other services, and growth in industrial and agricultural activity. Real GDP growth is projected to reach 5.6 percent in 2022, below pre-pandemic levels. In addition, the country remains vulnerable to the emergence of new COVID-19 variants (only 13.2 percent of Gambians are fully vaccinated), commodity price shocks, and weather-related risks. Inflationary pressures, particularly on food, are expected to remain high in the short term as global supply chain constraints continue to exacerbate structural issues at the Banjul port. Rising food prices will remain a burden for vulnerable households while increases in non-food inflation could dampen domestic demand. The current Russia-Ukraine war also heightens uncertainty given the Gambia's position as a net importer of food, fertilizer, and fuel. A protracted war could further exacerbate commodity price shocks and supply chain disruptions, especially global oil prices, fueling already high food inflation and worsening food insecurity.

3. The authorities' commitment to sound policy action and the continued implementation of reforms is critical to entrenching the gains from recent macroeconomic improvements. Improvements to the fiscal position in the medium term will rely on the Government controlling non-priority spending and limiting domestic borrowing, therefore strong public financial management, and governance reforms are critical. The outcome of the December 2021 presidential election further cemented the current administration's authority, which helps to support further implementation of reforms in various sectors. While political risks were moderated by successful and peaceful parliamentary elections in April 2022, governance risks remain high given continued complexity in the political economy as well as weak institutional and governance structures.[12] In addition, further delays to the constitution review process risk stirring political instability while heightening social tensions.

[12] World Bank Gambia Economic Update, June 2022

B. The Financial Sector

4. **The financial sector is small, and bank dominated.** Total financial sector assets were about 88.5 billion GMD at end-2021, representing about 85 percent of GDP. The banking system accounts for about 86 percent of total financial sector assets and is the main form of financial intermediation in the country. Other deposit-taking financial institutions or NBFIs include 3 deposit taking finance companies (FCs), 54 credit unions (CUs), and 69 active Village Savings and Credit Associations (VISACAs). In addition to rather small pension and insurance sectors, other financial services providers include 156 foreign exchange (FX) bureaus (many offering money transfers and remittances services), and two mobile money operators (MMOs). See Annex 1 for details. Outside of the tourism sector[13] and development partners, financial resources outside the domestic financial system are very limited or non-existent.

5. **The banking system is mostly foreign owned, highly concentrated, well-funded, and surprisingly larger than regional and country comparators.** There are 12 commercial banks (including 1 Islamic Bank) in the Gambia, most of which are foreign and privately owned.[14] Although all banks are domestically incorporated, three banks are domestically-owned, one is of UK origin, and the rest are pan-African banks – with four foreign subsidiaries of mainly Nigerian origin while others are of Ghanian, Guinean, Togolese, and Libyan origin. Bank concentration is high with four banks comprising about 65 percent of total assets and about 68 percent of total deposits in the banking system. Despite a low average income and low level of savings[15], bank deposits to GDP, a measure of bank funding, were about 50 percent at end-2021 and about 45 percent at end-2020, higher than the SSA median of 27 percent and the SSA LICs average of 26.5 percent.[16] Furthermore, banking penetration or total banking sector assets to GDP stood at 70.5 percent of GDP at end-2021, much larger than the Sub-Saharan Africa (SSA) region median at 53 percent of GDP while the SSA Low Income Countries (LICs) average is 47.2 percent of GDP.[17]

6. **Despite its funding attributes and its relatively large size, the banking sector is characterized by low financial intermediation.** Bank credit to GDP stood at about 9 percent at end-2021, significantly lower than the SSA median of 14.9 percent and the SSA LICs average of 14.6 percent. Additionally, the loan to deposit ratio at 17.5 percent in 2021, is far below the SSA median of

[13] The tourism sector relies heavily on International Tour Operators (ITOs) to source and access tourists to the Gambia. As a result, much of the funding for investment (mostly hotels) comes from these ITOs. See World Bank. 2020. The Gambia: Policies for Private Sector-Led Growth – Achieving Sustainable and Inclusive Growth. Washington, DC: World Bank.
[14] Only one bank is under CBG administration following its failure in 2015 and is majority owned by the government.
[15] Per World Development Indicators, GDP per capita was $692 (constant 2015 USD) in 2020 and the ratio of national savings to GDP was 32 percent in 2020.
[16] World Bank FinStats Database 2021.
[17] IMF SSA Regional Economic Outlook, April 2022.

67 percent and the SSA LICs average of 70.8 percent.[18] It should be noted that almost all intermediation is in domestic currency as serious issues with the exchange rate regime during the former administration raised foreign exchange (FX) risks for banks.[19]

7. Financial depth of the banking sector, and ultimately financial sector, is limited by structural challenges. While above average banking penetration and deposit levels are typically indicators of financial depth, extremely low financial intermediation indicators highlight a sector struggling to find worthwhile investment opportunities. As such, the sector is unable to play its role as an effective enabler of the Gambian private sector. Difficulties in intermediating funds in Gambia are largely explained by structural issues caused by low private sector development resulting in a particularly small private sector, long-standing problems with contract enforcement and foreclosures, and difficulties overcoming financial information asymmetries. The structure of banks' balance sheets is also holding back financial deepening. The industry's liabilities are almost entirely short-term, which helps to explain the lack of appetite for long-term financing to avoid large maturity mismatches.

8. Efforts to improve financial deepening have stalled despite efforts to reduce fiscal crowding out. Increased fiscal financing caused total private sector credit to GDP fall steadily from 11.7 percent in 2013 to 6.1 percent in 2017[20] while returns on government securities soared – yields on 91-day treasury bills reached a peak (in over a decade) of above 17 percent between July 2015 to June 2016.[21] This pushed lending rates to over 22 percent during this period. Private sector credit recovered in 2018 following better economic management policies in 2017 and a rapid decline in yields on government securities providing space for private sector investment. Although this ratio grew to reach 9 percent in 2021, it still compares poorly against peer comparison groups (see above). Similarly, the performance of other financial corporations, as measured by insurance company assets to GDP, has remained stagnant at about 1 percent since 2015, trailing the median for SSA of 5.7 percent and the SSA LICs average of 5.7 percent.[22]

9. Although aggregate financial soundness indicators show that the banking sector has ample liquidity and capital, these buffers could be limited given continued high exposure to the public sector. High ratios indicate a sector with ample liquidity, but these indicators may be misleading as government securities (the largest component of bank assets) are not particularly liquid

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[18] IMF SSA Regional Economic Outlook, April 2022.
[19] A series of ad-hoc presidential directives imposed fixed over-valued exchange rates during 2012-2015, the peg was lifted in early 2016.
[20] IMF SSA Regional Economic Outlook, April 2022.
[21] CBG data.
[22] World Bank FinStats Database, 2021 and CBG data.

due to the lack of a secondary market. At end-2021, the aggregate capital adequacy ratio was 29 percent, well above the 10 percent regulatory minimum. However, large holdings of zero-risk government securities (more than a third of bank assets) and the corresponding low share of risk-weighted assets boosts regulatory capital ratios, raising questions about the effective size of buffers to absorb shocks. See Annex 2 for Financial Soundness Indicators.

10. High exposures to the public sector make sovereign risk a source of vulnerability, particularly in the context of high public debt levels. As commercial banks hold the majority of government debt, this raise concerns regarding bank-sovereign nexus: direct exposures to the public sector makes banks' balance sheets vulnerable to losses on government asset holdings and the sovereign is often implicitly expected to support failing banks. These two channels may interact and give rise to feedback dynamics in which sovereign distress amplifies bank distress and vice versa. Further, during times of stress (for instance the impact of the pandemic), a strong sovereign-bank nexus can serve as an amplifier of shocks.[23] Following the political transition in 2017, the Gambia was in high debt distress. However, some good progress has been made to moderate debt levels, notedly through various debt relief initiatives with external partners as well as reprofiling (longer maturities at lower rates) and reducing domestic debt. As a result, the country exited high external debt distress, but public debt levels remain high at an estimated 83 percent of GDP at end-2021. Public debt is projected to stay on a downward path, declining to 64.4 percent of GDP by 2024, if fiscal consolidation is diligently sustained.

11. The NBFI sector is small, but critical for increasing financial inclusion in the Gambia. Most of these financial institutions, namely Credit Unions (CUs) and VISACAs, are small financial units primarily focused on traditional savings and loans products, particularly microfinance services. Total NBFI assets were about 4.7 billion GMD and less than 5 percent of GDP. According to the 2019 FinScope Survey, 5 percent of Gambians have a traditional bank account while 14 percent use services of a NBFI. In addition, many MSMEs utilize FCs and CUs for their financial services due to limited access to bank finance given the lack of available collateral, the lack of reliable financial records, and the informality of their businesses. Also, the main business of FCs is lending to women micro-entrepreneurs through the group financing model. In most rural areas, NBFIs are the only financial institutions with presence either through physical or mobile branches. As a result, these entities are critical to increasing access to financial services to unserved and/or underserved segments of the population.

[23] Giovanni Dell'Ariccia & Caio Ferreira & Nigel Jenkinson & Luc Laeven & Alberto Martin & Camelia Minoiu & Alex Popov, 2018. "Managing the Sovereign-Bank Nexus," IMF Departmental Papers / Policy Papers 18/16, IMF.

12. Long-term financial institutions are underdeveloped relative to peers. As of 2021, pensions assets account for 6 percent of total financial assets (5 percent of GDP), much lower than the SSA median of 8.5 percent of GDP. In addition, there is no pension regulator, and the financial performance of the main pension scheme (administered by the SSHFC) has been deteriorating in recent years. Independent financial analyses have shown that the viability of the country's social security system is at serious risk unless structural issues are addressed.[24] The insurance sector is small, comprised of 12 companies that represent about 1.3 percent of total financial sector assets (about 1 percent of GDP), much lower than the SSA median (as noted earlier). The sector faces many challenges and constraints and it is regulated by the Central Bank of Gambia (CBG), which lacks the specialized personnel to support growth and innovation. At present, there is no capital market, although there is a draft legislation in place to establish one.

13. The institutional investor base is dominated by the SSHFC, which has significant linkages to the rest of the financial sector which could generate serious financial risks. The SSHFC is governed by the 2015 SSHFC Act and administers four funds: i) two pension funds: the Federated Pension Scheme (FPS) and the National Provident Fund (NPF); ii) the Industrial Injuries Compensation Fund (IICF), and iii) the Housing Finance Fund (HFF). In total, the SSHFC manages total assets of 6.3 billion GMD (or 6 percent of GDP), which translates to about 7 percent of total financial assets. The SSHFC has substantial shareholding in two banks, including the second largest bank in the system. In addition, due to the lack of domestic instruments, SSHFC places a significant portion of its assets in term deposits within commercial banks. Following the collapse of the yields on government securities, demand for elevated returns on these SSHFC deposits affects the cost of funding for banks where these deposits comprise a substantial portion of their core funding. As an important investor in government securities, the SSHFC holds most of the 25 percent of government securities held by the non-bank financial sector. The sovereign-corporate nexus (discussed earlier) could amplify negative shocks in times of stress if the government’s perceived implicit guarantee of the SSHFC comes into question.

[24] See the Section VI for more details on the SSHFC.

III. BANKING SECTOR: VULNERABILITIES AND RISKS

A. Banking Sector Assessment

14. **Overall, the banking sector growth slowed during COVID-19 despite supportive central bank measures.** Nominal annual growth of assets, deposits, and loans dropped between 2019 and 2020, then rebounded in 2021. In real terms, growth shrank only for loans and deposits while asset growth remained positive mostly due to foreign exchange (FX) transactions and the enormous growth in formal remittances. In response to the COVID-19 shock, the CBG adopted an accommodative monetary policy stance to support the financial sector, notably: i) the policy rate was reduced from 12.5 percent at end-2019 to 10 percent by end-May 2020; ii) the reserve requirement ratio was lowered from 15 percent to 13 percent; iii) banks were advised to postpone dividend distributions; iv) emergency liquidity support was made available; and v) supervisory forbearance was applied on a strictly case-by-case basis.

15. **Banking sector vulnerabilities and risks also increased during this period.** As part of this FSAP, a banking sector assessment was conducted that builds on the IMF Financial Sector Stability Review (FSSR) conducted in November 2019 - see Annex 3 for key findings and recommendations of the FSSR. This assessment finds that the main sources of vulnerabilities and risks include deteriorating asset quality, funding concentrations, declining profitability, and longstanding structural issues. It stands to be reiterated that these vulnerabilities stem from the structure of the Gambian economy, including an undiversified economic base, overreliance on tourism and agriculture – that are both prone to external shocks - as well as macroeconomic weaknesses.

Deteriorating asset quality

16. **Asset quality deteriorated during the pandemic but is showing signs of recovery.** The average ratio of non-performing loans to gross loans (NPLs) increased from 4.5 percent in Q4 2019 to 7.7 percent in Q1 2021. Since then, NPLs have been declining to reach 5.2 percent at end-2021. As of December 2021, despite recent reductions, two banks (one small and one medium-sized) had notably high NPLS above 20 percent while three banks had NPLs above 10 percent high, much higher than the prudential guideline of 5 percent. NPLs ratios were highest in the building and construction, the distributive trade, transportation, and other commercial sectors. Thus, banks heavily exposed to these sectors, ceteris paribus, could be more vulnerable if economic conditions falter. Surprisingly, the

downturn in the tourism sector did not contribute to a large spike in NPLs in this sector. Less than 5 percent of NPLs were registered in loans to the tourism sector. This finding is largely in part to the fact that most investment in this sector is funded by International Tour Operators as explained in the previous section.

17. Loan loss provisions decreased despite worsening asset quality. The coverage ratio averages dropped from 90 percent for the entire system in 2018 to about 60 percent in 2019 where they have remained since. While the banks with the highest NPL ratios in the system tend to have above average provisioning levels, one bank with an NPL ratio above 10 percent has below average provisioning at end-2021. In addition, small banks tend to have provisioning levels that fall below the average for the system.

18. Provisioning forbearance measures on specific problem loans could further lower provisioning levels. One of the financial support measures adopted by the CBG was the relaxation in the realization of provisioning for certain loans that were clearly impaired by the impact of the pandemic. This waiver was only applicable on a case-by-case basis following a consultation between the banks and the CBG. Regulatory flexibility, however, did not affect loan classification standards. As a result, provisioning levels are lower than they should be for some banks. Lifting these measures could cause problems for some small banks which would have to sharply increase their provisions. To prevent a buildup of vulnerabilities and a provisioning shock, the CBG is advised to gradually repeal these supervisory flexibility measures going forward. This recommendation also applies to other supervisory forbearance measures are in place currently.

19. The loan classification and provisioning system could be improved to support efforts to enhance monitoring of emerging risk.[25] There is a basic regime in place governing loan classification and provisioning. However, CBG should strengthen monitoring of bank policies and practices in this area in addition to improving enforcement of classification and provisioning rules to ensure an accurate view on banks' earnings and capital. The CBG should also continue to provide banks with proper training on how to classify and provision for loans to ensure adequate capacity within financial institutions. More detailed instructions on banks' risk mitigation policies and practices are required. Moreover, the CBG should require all bank Boards to have credit committees, tasked with determining, and reviewing the adequacy of implementation of banks' classification and provisioning policies and practices.

[25] This assessment relies heavily on the findings and recommendations of the guided Basel Core Principles (BCP) self-assessment prepared as part of the World Bank's technical assistance program to strengthen banking sector stability

20. Stress tests planned for September 2022 are welcomed, but until then closer periodic examination of the financial situation of banks with high NPLs and/or a portfolio subjected to forbearance measures is needed. To better understand the magnitude of risks related to high NPLs and NPLs subject to supervisory forbearance, the CBG should enhance the monitoring of bank operations that could be at risk. It is now of vital importance to develop an early warning system (EWS) using forward looking indicators and analysis. In addition, the stress testing methodology should include assessments that measure banks' loss absorption capacity and capital adequacy. At same time, the CBG will need to guard against excessive risk-taking by banks as the economy recovers, by critically reviewing the growth plans of the banks at risk. Lastly, a detailed assessment of bank credit portfolios (especially in small banks and NBFIs) is needed to better understand the impact of withdrawing forbearance measures as well as lagged effects of the pandemic on these institutions. This assessment will provide necessary clarity on the specific legal and regulatory gaps as well as the required supervisory capacity to strengthen oversight of the system.

21. Banks could also be asked to develop problem loan mitigation strategies given difficulties in resolving NPLs. These strategies could help to moderate issues faced by banks in recovering impaired assets due to issues with contract enforcement and foreclosure (see Section IV for details). This is a short-term solution until banks can develop dedicated problem loan management units.[26]

Declining Profitability

22. Reduced investment opportunities, due to mostly negative rates in real terms on government securities, have negatively affected bank profitability. Concerted efforts by the current administration to address high debt service limiting fiscal space resulted in a rapid fall in rates on Treasury bills. The yield on 91-day Treasury bills fell from over 17 percent in mid-2016 to a record low of 3.6 percent at the start of Q4 2017. These rates have remained below 5 percent since, falling below 1 percent at end-2021.[27] Meanwhile, the policy rate was reduced from 23 percent in September 2016 to 15 percent in June 2017, and even further to the current level of 10 percent in May 2020. In a banking system that relied heavily on income from government securities, profitability levels were significantly affected. Return on assets (ROA) dropped from 3.3 in 2016 to 2.7 in 2017, and further to 2.5 by end-2021 while return on equity (ROE) dropped from 19.8 percent in 2016 to 16.3 in 2017 and

[26] There is no evidence that these units exist according to the guided BCP self-assessment.
[27] As of end-April 2022, 12-month inflation registered its highest level in two years: 11.7 percent.

has since improved to 19.9 percent. It should be noted that ROE is currently declining following a peak of 22.4 in 2020. While these numbers for the overall system may not be appear to be alarming, this trend over recent years is concerning especially as margins continue to tighten as explained further below. Only one bank reported losses at end-2021, but more banks may record losses as the impacts of the pandemic are fully registered by the banking system – notably the withdrawal of forbearance measures.

23. **Shifting bank operations to increase lending and improve profitability prospects is sticky, given high adjustment costs and structural issues.** Gambian bank operations have not changed much in response to falling interest rates. Yields on government securities have been below 5 percent since 2017 but a large portion (more than 35 percent) of assets remain oriented towards these investments. It should be noted that adjusting operating costs is a medium term undertaking as such a restructuring may require staff changes, implementing systems that increase efficiency, and reducing the footprint of "brick and mortar" branches. This adjustment is slowly underway in Gambia, but the pace of this transition is hampered by structural issues that increase the perception of credit risk.

24. **Lending has slowly increased particularly during the pre-pandemic expansion, but credit allocation remains concentrated amongst a few creditworthy firms, further compressing margins.** Given continued high risk-aversion, banks have focused their lending efforts on corporates and a handful of bankable small and medium enterprises (SMEs). Heavy competition for these firms has reduced lending rates offered to them, which has substantially lowered bank spreads.

25. **The CBG lending rate guidance of 15 percent acts as a de-facto interest rate cap, reducing margins significantly.** In 2020, the CBG issued a guidance to all banks to keep lending rates to a 5 percent spread above the policy rate in order to support economic recovery during the pandemic. With the policy rate at 10 percent, maximum lending rates on new loans cannot exceed 15 percent. Calculations of ex-post interest rates using bank financial statement data show that this lending guidance is binding for 5 of the banks in the system (Figure 1). This is because this lending rate ceiling does not consider different business models that could affect the cost of extending credit, e.g., lending to riskier segments that entails high overhead costs and risk premia that may be inadequately compensated by the current lending rate maximum. In addition, this lending rate ceiling may not sufficiently cover costs if the average cost of funding in a bank is high. For instance, SSHFC deposit placements command a return close to the highest yield on government securities (about 8 to 9 percent), which drives up the average cost of funding. As such, banks with larger shares of SSHFC deposits may struggle to cover their costs under this lending rate guidance. Indeed, one small bank

with large shared of SSHFC deposits is unable to meet its costs using the current lending rate guidance.

26. The CBG should withdraw this lending rate guidance given its impact on lending, particularly to economic segments that already struggle to access finance. Although bank data shows that lending in the system increased overall in 2021, four banks (including the largest bank) have reduced their lending in 2021 despite favorable economic conditions. For 3 of these 4 banks, the lending rate guidance is binding (Figure 1). Discussions with banks during the missions further confirmed these trends. The most concerning finding was that some banks reported curtailing lending to certain segments that carry high credit risks, such as agriculture and MSMEs, due to this guidance. This guidance is financial repression[28] that aggravates an already challenged financial sector, compounding issues of low intermediation, inclusion, and development. Moreover, it introduces a financial distortion that significantly limits the number of instruments that development partners can provide to support financial sector development in the Gambia.

27. Small banks are most vulnerable to the continued trend of declining profitability. Large banks tend to have more buffers and are less likely to struggle raising capital from parent banks, if needed. Small banks in the system have smaller buffers and risk becoming non-viable if these conditions persist. One small bank that has struggled to make profits in recent years could fail if the bank business model is not adjusted in the short term. These findings further strengthen the call for a detailed assessment of bank lending operations to ensure the adequacy of necessary buffers.

Concentration risks

28. High concentrations of SSHFC deposits in funding portfolios pose systemic risk. Given the small size of the Gambian economy and its undiversified nature, there is a very limited number of entities that offer good business opportunities to banks, both from the liability and asset side. With regards to liabilities, SSHFC deposits comprise between 11 and 31 percent of the total deposits in four banks. Dependance on these deposits may not only form a liquidity trap for these banks but may also impede the SSHFC's ease of withdrawal at maturity. Moreover, as noted earlier, the SSHFC's demand for returns (comparable to the highest yields on government securities or more) adversely affects the

[28] Financial repression refers to the notion that a set of government regulations, laws, and other non-market restrictions prevent the financial intermediaries of an economy from functioning at their full capacity. Economists have commonly argued that financial repression prevents the efficient allocation of capital and thereby impairs economic growth. See Hiro Ito, 2008, "Financial Repression" The Princeton Encyclopedia of the World Economy, Princeton University Press, edited by Kenneth Reinert and Ramkishen Rajan.

average cost of funding. This is particularly the case for small banks where these deposits constitute a substantial portion of their core funding.

29. There is scope for CBG to enhance its monitoring and regulation of large deposit exposures. The CBG will need to monitor the financial condition of banks that have significant deposits from the SSHFC. In addition, the supervisor should consider conducting a horizontal review of concentration risk to detect any vulnerabilities across the system. The CBG should also consider regulating these deposits by adding a limit on these placements. This limitation is particularly necessary as the SSHFC does not have an investment policy in place, therefore they likely do not regularly conduct necessary prudential checks as part of their procedures to vet placements. As mentioned earlier, a more detailed assessment of bank operations is required to better understand the necessary remedial actions needed to strengthen bank risks to these vulnerabilities. This assessment should take the SSHFC investment policy that is under-draft into consideration, see Section VI for more details.

Long-standing Structural issues

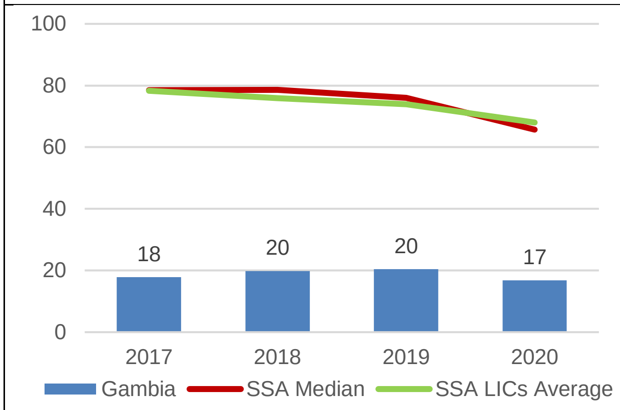
30. Structural challenges have persistently hindered bank financial intermediation in the Gambia. All banks cite financial information asymmetries and weak contract enforcement as well as foreclosure issues as significant obstacles to their ability to intermediate more funds. Mechanisms designed to alleviate information asymmetries remain inefficient and ineffective, notably the credit reporting service provided by the Credit Reference Bureau (CRB). Secondly, weak enforcement of creditors' rights mainly due to the fragmented legal framework, lengthy court proceedings, and difficulties in enforcing judgements to foreclose severely hamper banks' attempts to take possession and liquidate collateral, undermining NPL resolution. This, in turn, raises bank risk aversion and is translated into higher risk premia and higher costs of credit. (See Section IV for details).

31. Urgent solutions are required to address these longstanding structural issues, particularly to tackle the issue of low financial intermediation. To this end, the CBG is advised to engage the Ministry of Justice (MoJ) to expedite efforts to re-establish specialized commercial courts that can fast track the enforcement of contracts.[29] In addition, it is important to strengthen mechanisms that facilitate the collection of financial information (see Section IV for more details).

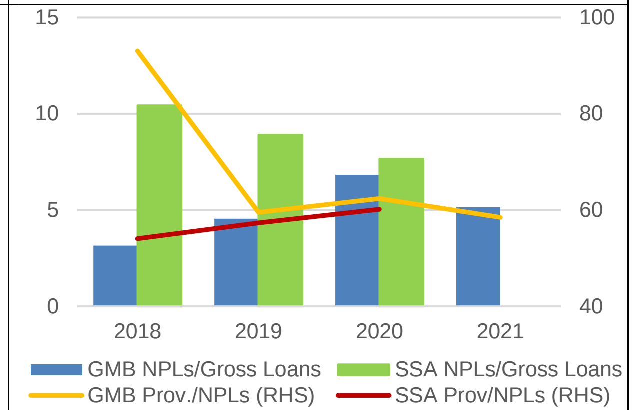
[29] This recommendation reiterates similar calls by the IMF in the December 2021 Article IV.

Figure 1: Select Banking Sector Indicators

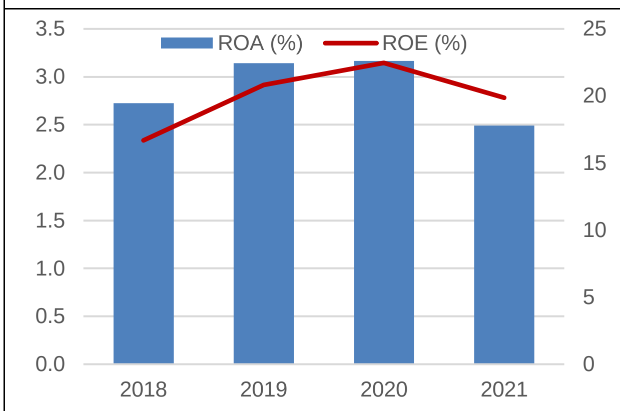
Loan to deposit ratios highlight persistently low levels of financial intermediation



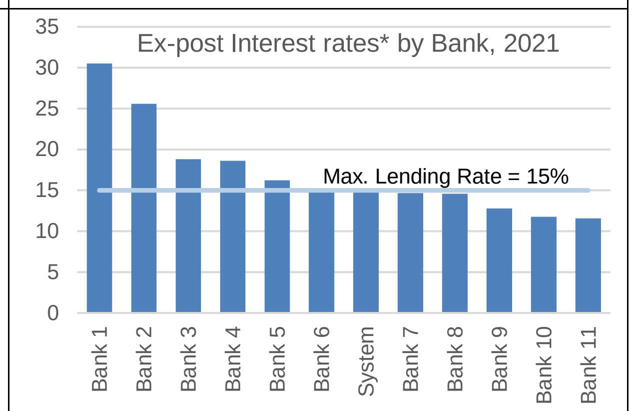
NPL Ratios increased while provisions decreased…



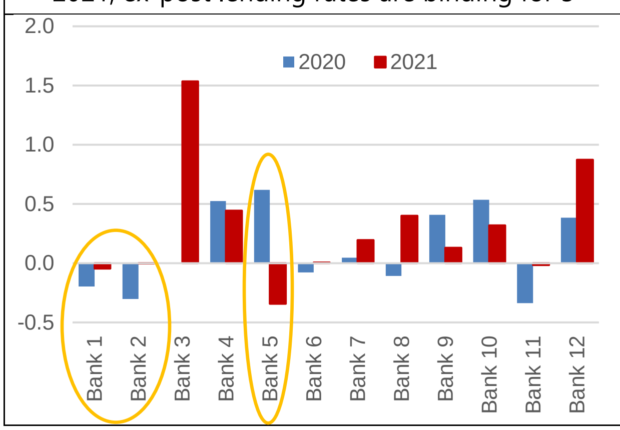
…and profitability has come under pressure



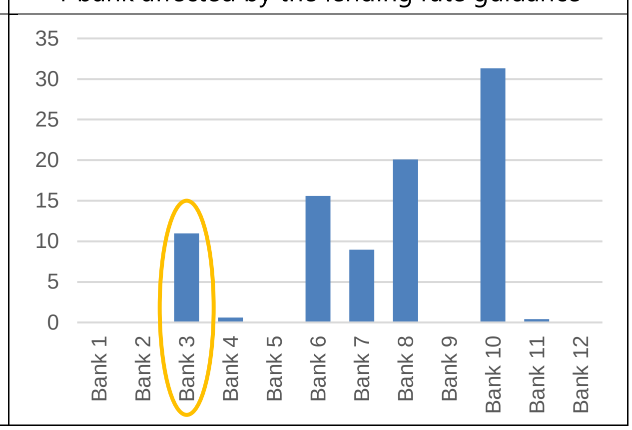
The interest rate guidance appears to be binding for 5 of the banks, 2 of which are small



Lending growth rates were negative for 4 banks in 2021; ex-post lending rates are binding for 3



SSHFC deposits pose concentration risks, even in 1 bank affected by the lending rate guidance



Sources: CBG; WB FinStats 2022, WB FSAP team calculations, IMF SSA Regional Outlook, October 2021

* Effective (ex-post) lending rates calculated using balance sheet data (interest income on loans to average net loans)

B. Banking Sector Legal, Regulatory and Supervisory Issues

32. Similar to the banking sector assessment, this section builds on the IMF FSSR. The findings below consider recommendations provided by the IMF FSSR and the CBG FSSR Strategy Plan.

Banking Act and secondary legislation

33. The CBG's independence is challenged in the Banking Act.[30] The Minister of Finance can make regulations to empower the provisions of the Act, including the provision of penalties for breach of any of the regulations. The Minister may also exempt any person or a class of people from the whole or any part of the Act (as agreed by the CBG and the Minister). In addition, the Minister may designate any type of service as a banking business or may certify that issuing a license would not be in the public interest, causing the CBG to deny a license application. It is recommended that the CBG, particularly the supervision activities, have in arm's length relationship with the Minister.

34. The Banking Act does not describe ultimate beneficial owners (UBOs). Information on UBOs assist the supervisor in correctly identifying parties related to the bank in order to determine the risk groups to which direct/indirect credit exposures will be calculated. CBG is recommended to obtain information from the banking institutions indicating the shareholding structures of the legal entity founders until the real person shareholder or partners (UBOs) are reached.

35. Per the Banking Act, the CBG may take corrective measures on a problem bank, but these actions can be challenged if not explicitly backed by the legislation. The Act does not explicitly list the corrective measures that the CBG can take. Rather, the CBG is given a free hand to decide the measures as long as they will ensure the resolution of problems at the earliest possible time. However, this approach opens the door to challenges on CBG decisions by banks and their shareholders. To avoid such legal challenges and delays, the Banking Act should clearly authorize the CBG to employ a wide range of explicitly stated preventive, corrective and restrictive measures.

36. Application of recommended prompt corrective tools requires a strong risk management and internal control system, an effective internal audit function, an influential corporate governance and quality reporting in banks. First and foremost, the CBG has to compel the banking institutions to develop internal risk management and control systems and assign duties

[30] Similar situation exists for the NBFIs. (NBFIs Rules and Guidelines on Policies and Procedures – Volume Six)

and responsibilities accordingly starting from the Board of Directors. Within this context, the banking institutions should be requested to form Risk Committees at board levels and risk management functions within the banks. External auditors should report on the quality of risk management, internal audit and internal control systems in their reports.

37. **Triggers for the intervention in a bank are unclear.** The CBG is authorized to take possession of a banking institution, but the triggers are vague and legally disputable definitions like, "unsound condition", "imprudent manner". There is a need to clearly define these triggers. Moreover, corrective actions, triggers for intervention and handing over the problem banking institution for resolution and sanctions to be applied should be grouped together in the order listed here within the Banking Act.

38. **Meanwhile, the CBG is allowed to capitalize an intervened troubled bank, which is not advisable by international standards.** The balance sheet of the CBG should not in general be used, partially or wholly, to invest in banks. The resolution framework should rather call for a government agency to be in charge of such capitalizations (nationalization).

39. **There is no formal bank resolution framework in The Gambia despite difficult experiences with failed banks in the past.** The CBG has overseen 2 major bank resolutions in recent history which were costly, took too long, and weighed down central bank balance sheets. The CBG can take over a bank or request its compulsory liquidation according to the Banking Act. The reorganization powers for intervened banks do not full align with internationally recommended tools. A new and more organized resolution framework keeping the process outside the general bankruptcy system, would further clarify bank resolution. The Act may be amended to: i) clearly define the associated tools, such as bridge banks, purchase and assumption transactions, nationalization, bail-ins, etc.; ii) include requirements for resolvability assessments and financing the implementation of the resolution plans; iii) describe removal of impediments to resolvability; and iv) define the resolution administration including its duties, responsibilities, authorities and supervision. A new and comprehensive bank resolution framework should also address the potential cross-border resolution issues as well as the cooperation and coordination between resolution authorities in such situations.

40. **Given the issues outline above, the Banking Act should promptly be reviewed.** Amendments where necessary, should provide more clarity and define CBG's authority, regulatory tools, their powers and the approving bodies before they are formally enacted.

41. **Similarly, the CBG regulations, guidelines and directives should be reviewed to ensure their alignment with the amended Banking Act.** In this context, definitions of beneficial ownership, related and associated parties, establishment of risk management systems in banking institutions, introduction of temporary administration to problem banks, detailed description of additional resolution tools, defining the rules of preparing recovery and resolution plans to be requested from banking institutions, improving communication and coordination with cross-border supervisory and resolution authorities need to be addressed.

42. **The power of secondary legislation is not defined in the Banking Act and their enforceability remains unclear.** The legislation for banking institutions is based on the Banking Act, complemented by CBG guidelines, instructions, letters and reporting forms. The status and powers of these instruments are not defined in the Act, and their enforceability is not always clear. Neither does the Act set out what regulatory instruments can be issued by whom, nor does it clarify the issuance procedures. Clear authorizations secured by the Banking Act will only help the CBG decision makers, since their decisions will in most of the cases be subject to legal challenges.

43. **Although no bank has requested emergency liquidity assistance (ELA), there are no internal regulations governing this program.** The CBG Act authorizes the CBG to extend ELA facilities to solvent banking institutions against collateral for a period not exceeding 91 days. The CBG should issue a regulation governing the conditions of responding to ELA requests, including the financial position of the borrowing institutions, acceptable collateral, maturity and interest rate. It is also important for the CBG to coordinate with cross-border central banks and supervisors in order to set the responsibilities and principles of providing ELA to subsidiaries in Gambia.

44. **The CBG should make it compulsory for all banks and large NBFIs to have a contingency planning framework in their liquidity risk management policies.** The CBG monitors the liquidity conditions of the banks and large NBFIs. However, given the lack of a secondary market and the sizable share of government securities in banks' assets, the CBG is advised to run a cross banking sector liquidity analysis, with and without Treasury bills in the balance sheets. In addition, the CBG and the Ministry of Finance and Economic Affairs (MoFEA) should develop an emergency redemption mechanism in case ELA limits prevent the CBG from lending against Treasury bills.

45. **Some banks struggle to submit accurate and timely financial returns, affecting the work of the supervision department.** Some banks submit incorrect forms, which are send back for correction, and some banks submit late returns. Low penalties or leniency on the part of the CBG likely lead to banks taking this obligation lightly. The returns are prepared both in soft and hard copies. The

most efficient and secure solution would be to have the banking institutions incorporate reporting requirements into their core banking systems.

Crisis Management and Preparedness

46. Ensuring financial stability and soundness, including preparing for and managing a financial crisis, is not the sole responsibility of the CBG. Maintaining financial stability at all times, identifying and preparing for a crisis, improving the legislation and the framework of tools to handle systemic risks, establishing credibility and restoring confidence in the banking sector, and establishing a single channel of communication used by all relevant crisis-management agencies requires the participation of all institutions that would be expected to take part in safeguarding the financial sector. This interagency collaboration should either be governed by a law or a Presidential decree[31], which would outline the principles of cooperation and ensure information sharing. In other countries, this entity is typically the Financial Stability Council (FSC), (or Board or Committee). In the Gambia, this council should include: the CBG, MoFEA, SSHFC[32], and, in the future, the Deposit Guarantee Authority (DGA).

47. Limited regular technical dialogue between the CBG and MoFEA is problematic. These institutions currently only communicate at senior management level. In addition, MoFEA does not have a unit responsible for overseeing financial sector development. Institutions that play vital role in maintaining financial stability should be able to effectively communicate and share information at technical expert levels as well.

Safety Nets

48. There is no deposit insurance system in place in The Gambia. Introducing a deposit protection mechanism for all banking and non-bank financial institutions authorized to accept deposits, should be considered only after ensuring that the quality of supervision is at internationally accepted levels and that all failing institutions have been resolved.

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[31] For example, Türkiye, Croatia, Denmark, the Netherlands, Hong Kong SAR, China, Ukraine, Azerbaijan, Tajikistan preferred law or presidential decree; some others like Albania, Switzerland, Sweden, UK signed MoUs among the FSC members.
[32] SSHFC is recommended to be a member of the FSC due to its linkages with the financial sector.

Strengthen Banking Supervisory capacity

49. CBG plans to establish a Financial Stability Unit (FSU) by the end of Q2 2022 are welcome. The FSU could act as the Secretariat of the FSC, when and if the latter is established. In addition, the FSU should coordinate the development of macroprudential policies and tools.

50. The examiners of the FSD handle multiple tasks that can give rise to conflicts of interest. In addition to bank examination, they decide on the measures to be taken by the banking institution, ensure timely enforcement of these measures, propose sanctions for those in violation, and, on an ad-hoc basis, they participate in internal working groups used to develop regulations and guidelines. Development of regulations, guidelines, and keeping up to date on international standards in this area needs experience, expertise and concentration. It is recommended that the CBG establishes a Regulations/Methodology Unit, to be staffed by 2-3 people, who focus on the development of regulations and supervisory methodologies.

Cross border Supervision and cooperation

51. The banking sector's ownership structure (majority foreign-owned) requires a more fit-for-purpose bank supervisory framework. The CBG currently relies on the West African Monetary Zone (WAMZ) supervisory college to conduct cross-border supervision and facilitate cross-border cooperation for supervising the foreign banks in the system. While this working arrangement has not created major issues so far, its effectiveness will only be tested when cross-border weaknesses must be readily managed, i.e., when swift and efficient communication and information flows are needed in the event a rapid-response situation emerges. As such, the CBG should start working directly with supervisors of parent banks to develop specific action plans aiming at resolving parent/subsidiary weaknesses that will: i) include ex-ante burden sharing mechanisms, ii) give strong powers to close or restructure banks, iii) limit the potential burden on taxpayers, including by "bailing in" creditors as necessary, and iv) support market discipline beyond receiving prudential and stability indicators on parent banks from their supervisors.

52. There is no framework in place to facilitate cooperation in cross-border resolutions. However, the College of Supervisors of WAMZ is working on a draft bank resolution framework. The Banking Act should be amended to give a wider range of cooperation and exchange of information powers to the CBG with home supervisors and resolution authorities, including sharing recovery and resolution plans of the banking institutions and their parents. The CBG should retain the legal powers to intervene in and resolve problem banks within their jurisdiction, if cross-border cooperation fails. In addition, differences in national resolution frameworks will need to be harmonized to build an effective crisis management framework.

53. It is important that the CBG work with parent banks' supervisors and resolution authorities in the preparation of contingency resolution plans. The CBG and the cross-border supervisors should explicitly define and inform each other on their resolution powers and responsibilities, be flexible to respond to individual cases, ensure that they can exchange information, and that legal powers and all resolution tools exist. The resolution framework should enable the resolution authority to share non-public bank information with foreign resolution authorities on reciprocal basis, on time with no delays. Performing crisis simulation exercises, which also explore how to ensure continuity of a banking institutions' payment and settlement functions periodically, will help increase the quality of cross-border cooperation.

IV. MSME ACCESS TO FINANCE AND FINANCIAL INCLUSION

A. MSME Finance

54. Access to credit by micro small and medium enterprises (MSMEs) remains challenging in Gambia. Only a small number of MSMEs have access to finance either formal or informal (20% according to the latest available MSME Mapping Study).[33] According to the World Bank's Enterprise Survey, 72 percent of small and 40 percent of medium-size firms cite access to finance as a major constraint to their growth. Further, only 10 percent of small and 12 percent of medium-size firms have access to (bank) credit, which compares poorly to the Sub-Saharan Africa region findings of 16 percent and 26 percent, respectively. It is difficult to get current data on MSME lending since there are no disaggregated data available. However, anecdotal feedback suggests that only a tiny fraction of banks' loan portfolio is allocated to MSMEs.

55. Beyond banks, MSMEs access formal financial services from the NBFI sector, which often lacks capacity to lend and the propensity to innovate, among other inefficiencies. Financial leasing, factoring, financial technology (fintech) or other companies offering alternative or innovative credit products to small businesses have not yet significantly moved into the market. At present, many CUs and VISACAs struggle to be financially viable and, in many cases, are reliant on donor funding.

[33] GIEPA 2018

Difficulties accessing long-term and low-cost wholesale funding limits most NBFIs' ability to provide credit, including longer-term credit to microenterprises needed for fixed investments. Although some wholesale funding was available through the Social Development Fund (SDF), these resources were not enough to meet the demand. Given a number of these issues, NBFIs have limited incentives to innovate and to better serve the MSME sector. Moreover, little competition between these entities and banks (particularly small banks), given market segmentation based on the different products and services provided, disincentivizes efforts to become efficient and to innovate.

56. Any credit available to MSMEs comes with a high price tag. Banks charge most MSMEs the maximum 15 percent interest rate (per the interest rate guidance – see Section III for details). Alternatively, NBFIs charge even higher interest rates as they struggle to access cheaper funding and they are not subject to the interest rate guidance. As mentioned earlier, this guidance further constrains difficult MSME access to finance as the maximum allowable interest rate (15 percent) is perceived to be too low to allow appropriate risk benefit pricing.

57. Demand-side challenges to MSME access to finance include a high level of informality, unreliable financial management and reporting, and overall low levels of financial literacy. Most MSMEs in the Gambia operate on an informal basis. These firms often do not declare taxes or employees and mainly transact in cash. Informal businesses generally have lower productivity than formal businesses, which impedes both firm and economic growth. A number of these characteristics of informal firms make it difficult for formal financial institutions to properly serve these firms. In addition, the lack of business acumen and general financial literacy affects the reliability of financial books, even for formal businesses, and in turn limits their access to finance. When banks are unable to rely on firm financial records, information asymmetries increase along with the costs of doing business. Together, these factors raise the perception of risk in banking MSMEs which, in turn, raises the cost of credit to MSMEs.

58. More investment in business development services and financial education for entrepreneurs or MSME managers should be a priority. Financial literacy programs coupled with an introduction to financial consumer protection enable individuals to: i) make well-informed decisions on how best to use financial services; ii) build trust in the formal financial sector; and iii) contribute to healthy and competitive financial markets. To support the development and uptake of innovative products (as discussed in Section V), authorities could also develop MSMEs' financial accounting capabilities, such as by building on Gambia Investment and Export Promotion Agency's (GIEPA) current MSME support efforts and gradually introducing cloud-based accounting as well as an e-invoicing platform and services.

59. A credit reporting system is available, but further strengthening of the system is needed to increase its usage and to efficiently improve information asymmetries. The CBG set up the CRB in 2008 and it is available to all banks. While the enforcement of bank reporting obligations has improved over the recent years, more are needed as the reliability and usability of the registry data remains poor - undermining the purpose of the CRB. The NBFI sector still has no access to the bureau and its credit data are not included in the system. By excluding this data, the CRB limits its potential to play a role in graduating smaller enterprises to the banking sector from NBFIs. In addition to NBFI data, the CRB should explore collecting data from other entities that provide credit or post-pay services.[34] The credit reporting regulatory framework is also incomplete, creating potential data privacy and security risks for consumers. A credit information law or a data protection regulation would address these issues.[35]

60. Using collateral for risk mitigation is severely undermined by systemic issues surrounding land ownership, registration, and enforcement. Lenders generally prefer immovable collateral. Because most MSMEs only have movable assets to offer as collateral, this creates a collateral gap. The collateral market is regulated by a spectrum of laws including the State Lands Act, The Mortgages Act, The Gambia Tourism Authority Act and the 2001 Land (Registration of Deeds) Act. The poor state of land titling, interplay of various laws, and the complexity of customarily ownership (especially outside the Banjul area) further complicate lending against property and negatively influence the valuation of properties in general. In addition, there is no electronic database for checking for encumbrances (liens, mortgages, restrictions) nor one for recording boundaries, checking plans and providing cadastral information (geographic information system). Further, the procedures for land registration tend to be cumbersome and time consuming. Lastly, a suboptimal system of creditors rights enforcement severely affects collateral valuation and contributes to the perception that lending in Gambia is very high risk.

61. Although a secured transactions system for movable assets has been in place since 2014, many more efforts are needed to increase its uptake and usage. A shallow secondary market represents a serious constraint to the re-sale of repossessed collateral, causing liquidity and valuation issues. As such, financial institutions that take moveable collateral (e.g., machinery and other productive equipment) use it as a moral pledge rather than mitigating risk using its economic value. Moreover, market participants report issues with the reliability of the IT system supporting the registry.

[34] Possible sources include: SDF, Women's Enterprise Fund (WEF), the two mobile money providers, National Water and Electricity Company (NAWEC) post-paid services, and retailers that provide credit.
[35] A national data protection and privacy bill was drafted in 2019-2020, but it has yet to be passed into law.

Improvement of the implementation of a secured transaction in movable asset reforms can increase the pool of assets available for use in securing financing, balance the immovable/movable asset collateral mix of financial institutions, and support the emergence of an inclusive and strong financial system that supports private sector development in Gambia.

62. In addition to long-term comprehensive land reforms, short to medium term efforts to improve lenders' ability to mitigate risk include strengthening judicial capacity, increasing moveable collateral awareness, and considering potential regional solutions. Enhancing the capacity of the judiciary to adjudicate commercial disputes and to increase the efficiency of the enforcement process helps to reduce the high costs of recouping losses by claiming collateral. Meanwhile, improving market sensitization about the movable collateral system can help to raise the perceived value of this collateral, and, in turn, increase its acceptance and usage. Also, exploring opportunities to leverage the ECOWAS region to deepen the secondary market for repossessed movable collateral could improve liquidity and valuation problems. A regional e-commerce platform for sale of certified assets could be a possible solution.

63. Other key supply-side challenges include undiversified financial products, an incentive structure that entrenches the MSME finance market failure, and the lending rate guidance for banks. Firstly, the Gambian financial sector needs more innovative financial products to better serve MSMEs.[36] Most financial services providers in the country offer more traditional lending products with short maturities, which are mostly inadequate at supporting MSME investment or too expensive to accommodate their working capital needs. Additional efforts are needed by financial institutions to build their capacity and understanding of new products as well as to realize the potential of the movable collateral system and digital financial services. Secondly, this assessment highlights a wide gap between the offerings of Gambian financial services providers and the financing needs of Gambian MSMEs. Despite falling profitability described in Section III, there are very limited incentives to push financial institutions, particularly banks, to bridge this gap. Given the lack of a private sector entity in the market to demonstrate success in MSME financing, this push will not be a naturally occurring phenomenon in the Gambia. Therefore, government policies are needed to address this market failure. Lastly, the lending rate guidance that sets a maximum lending rate of 15 percent further exacerbates this situation as the lending rate ceiling may not sufficiently cover costs for the riskier clientele.

[36] These products include; accounts receivable finance (factoring), secured revolving lines of credit, financial leasing or peer-to-peer lending

64. The NBFI regulatory framework needs revisiting to introduce risk-based regulation and to create an environment that is supportive of innovative financial firms and the diversification of products. The NBFI 2016 Act and the implementing regulations need to be updated and modernized. The updated legal and regulatory framework should distinguish between microfinance development finance and purely business-oriented finance. Public funding and other subsidies should be directed exclusively through development finance. In addition, this framework should introduce licenses and regulatory requirements for financial leasing, factoring and platform-based finance.[37] Further, authorities could consider introducing measures to make these financial products more viable, e.g., an electronic invoice system and regulations on maximum payment terms for government-to-business (G2B) and business-to-business (B2B) payments to MSMEs. A specific regulatory approach to fintech innovation is also missing especially as these companies are showing interest in entering the Gambia market. The 2011 Regulation for the Provision of Mobile Money Services would also benefit from revision as discussed in Section V. As part of this legal review exercise, the prudential rules (capital adequacy, liquidity, and reserve requirements) should be reconsidered to properly respond to the risk of different financial services as encouraged by international standards.

65. An updated regulatory framework and ensuing guidelines are critical to efficient market development and to increased investor appeal. Without these regulations and guidelines, firms struggle to understand the "rules of the game" or the legal and regulatory requirements that affect their operations. A clear set of rules also provides transparency and clarity that facilitates investment decisions, increasing a country's appeal as an investor destination. Additionally, establishing an Innovation unit at the CBG (e.g., under the other financial institutions (OFI) or the payments systems department) is an important step to stimulate further development of innovative finance products by the fintech sector.[38]

66. Meanwhile, a well-established credit enhancement fund could incentivize financial institutions, particularly banks, to increase lending to MSMEs. In the absence of a private sector market innovator focused on MSMEs to generate a push and signaling effect, private-public sector partnership options could be used. Changing the incentive structure could be potentially accomplished by introducing a credit (finance) enhancement fund offering partial credit guarantees, matching grants for equity investments, and second-tier lending (wholesale funding). To successfully incentivize banks while avoiding moral hazard and adverse selection, a partial credit guarantee scheme (PCG) should: i) be well financed (liquid); ii) be well governed, based on international good

[37] A peer-to-peer lending service that can potentially replace and formalize traditional informal lending groups.
[38] A good example is the Bank of Ghana Fintech and Innovation Office.

practices (grounded in a law or a regulation); and iii) have a straightforward, transparent, and efficient claim management rule. The CBG is advised to ensure that these principals are incorporated in the PCG or credit guarantee scheme (CGS) that it is developing with support from the United Nations Capital Development Fund (UNCDF). Further analysis of these mechanisms and their feasibility for the Gambian market is required to determine the best course of action.

67. The proliferation of public sector funds to improve access to finance should be evaluated and a single structure should be considered, including to provide the proposed credit enhancement fund. SDF launched a youth focused revolving loan scheme in 2018 in partnership with the Youth Empowerment Project (YEP) funded by EU. Recently, a Women's Enterprise Fund (WEF) was established to address limited access to finance for women while GIEPA plans to set up a fund to improve MSME access to finance. Gambian authorities should evaluate this dispersion of funds and consider creating a single structure to achieve positive economies of scale and to increase efficiency. A possible solution could be to consolidate all the funds as separate financing windows under one umbrella development finance institution. SDF could be considered for this purpose as it was established in 1998 and has already invested in duplicable fixed overhead costs. The earlier proposal to assess the feasibility of a credit enhancement fund, mentioned above, should also consider how best to address this proliferation of public sector funds.

68. To address longer term and early-stage financing needs, the Gambian diaspora could be leveraged. The Gambian diaspora is known for its close ties with family that are in-country as evidenced by the high volume of remittances among other examples. These ties present an opportunity to create an ecosystem for providing longer term finance for SMEs and early-stage finance for start-ups. Further assessment is required to determine the best mechanism to engage the diaspora in developing alternative investment sources, however this is a longer-term undertaking given the lack of a capital market and underdeveloped business development services.[39] Creating synergies between local angel investors and providing matching grants schemes can be considered in the medium term. In addition, efforts can be made to explore ways to promote direct lending by the diaspora to Gambian businesses through Peer-to-Peer lending platforms. A more short-term feasible action, as well as a gateway to developing this ecosystem, is to make promoting local investment opportunities to the Gambian diaspora a regular part of government development policy activities.

[39] World Bank. 2020. The Gambia: Policies for Private Sector-Led Growth – Achieving Sustainable and Inclusive Growth. Washington, DC: World Bank.

69. Collecting data on MSMEs is also a critical step to addressing bottlenecks in providing access to finance to these firms. The CBG should start collecting data from banks and NBFIs on MSME finance using a uniform definition. At present, financial institutions use very different definitions of MSMEs, which adversely affects data collection, analysis, and the development of effective MSME finance strategies. The MSME mapping study planned for late 2022 by the Ministry of Trade, Industry, Regional Integration and Employment (MoTIE) presents a good opportunity to develop a new uniform definition. Also, the implementation of the recently launched National Financial Inclusion Strategy (NFIS) will provide ample occasions to engage the financial sector to begin this data collection.

70. Close coordination and cooperation between public sector stakeholders and private sector institutions are critical for the successful implementation of proposed recommendations. Public institutions, such as MoFEA and CBG, need to identify, prioritize, and sequence concrete actions to improve credit infrastructure, to revise financial sector laws and regulations, and to set up effective credit enhancement mechanisms. Positive outcomes hinge on the selection of the most appropriate public entities to implement these actions in coordination with private institutions (banks, NBFIs, mobile network operators (MNOs), and fintechs).

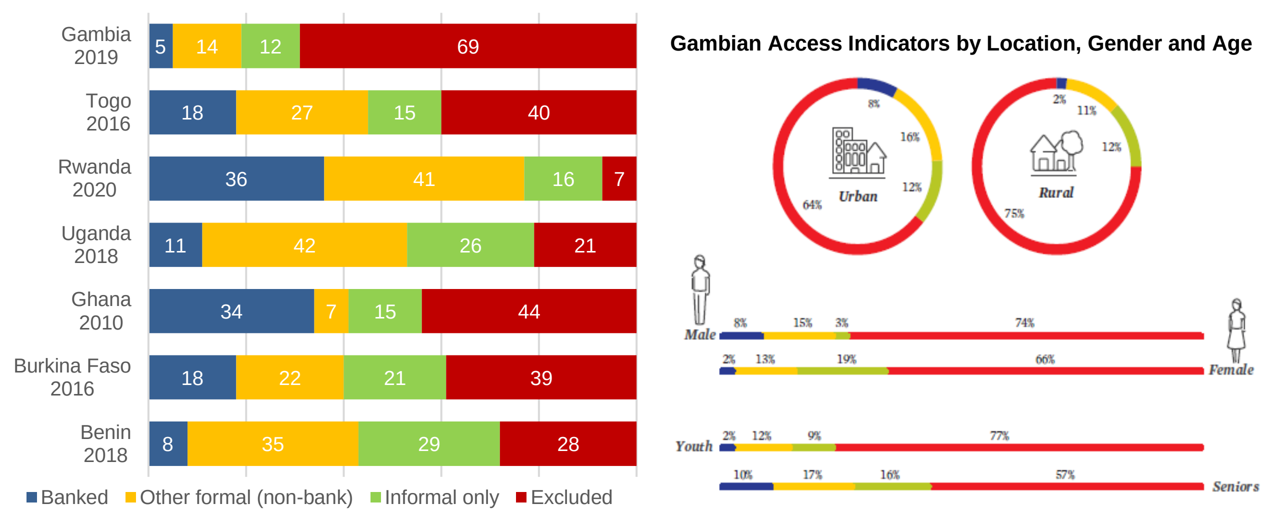
B. Financial Inclusion

71. The Gambia has one of the lowest levels of access to formal financial services in SSA. According to the FinScope survey, only 19 percent of Gambian adults are formally served by the financial sector (Figure 2). This is much lower than comparison peer countries such as Togo, Benin and Burkina Faso which report 45, 43, and 40 percent of adults with access to formal financial services, respectively as well as the LICs average (65 percent without access to an account) and SSA region average (57 percent without access to an account). The breakdown of the access indicator shows that access to formal financial services is much lower for those in rural areas (13 percent versus 24 percent in urban areas), women (15 percent versus 23 percent of men) and youth, aged between 15 and 35 years (14 percent versus 27 percent of those older than 35). Further, of the adults who use formal financial service providers, a low share uses more sophisticated formal financial services, such as credit (2 percent), savings (3 percent), and insurance is almost non-existent (only 0.5 percent).

72. Compared to comparator countries, The Gambia has a large number of adults that are financially excluded. Almost 70 percent of Gambian adults do not use financial services and products from formal and informal services, much larger than comparison and aspirational peer countries (Figure 2). The share of Gambian adults excluded from the financial sector is more pronounced for those in rural areas (75 percent) and for youth (77 percent). Meanwhile about 12 percent of adults use financial products and services from informal financial mechanisms that are not regulated, for instance osusus[40], teklas[41], local shopkeepers and money lenders. More Gambian women (19 percent) rely on informal financial channels compared to the overall adult population. As a result, women (34 percent) tend to be more financially included than men (26 percent). These indicators highlight that there is scope for formal financial services to expand and grow by better targeting women, youth and those living in rural areas.

Figure 2. Select Financial Inclusion Indicators

A. Share of Adults with Access to Financial Services in Gambia and Selected Peers



B. Geographic Outreach Indicators (Banks and NBFIs), 2020

	Number of commercial bank branches per 1,000 km2	Number of commercial bank branches per 100,000 adults	Number of ATMs per 1,000 km2	Number of ATMs per 100,000 adults
Gambia	**9.7**	**7.2**	**11.6**	**8.6**
Burkina Faso	1.2	2.8	1.9	4.4
Benin	2.1	3.4	2.8	4.5
Senegal	2.6	5.2	3.2	6.4
Togo	5.0	5.5	5.9	6.5
Uganda	3.0	2.4	4.8	3.9
Nigeria	5.7	4.4	20.7	16.1
Ghana*	7.0	8.5	9.4	11.5
Rwanda	14.6	4.6	13.5	4.3

	Number of MFI branches per 1,000 km2	Number of MFI branches per 100,000 adults	Number of credit union and credit cooperative branches per 1,000 km2	Number of credit union and credit cooperative branches per 100,000 adults
Gambia	**4.9**	**3.7**	**11.3**	**8.4**
Uganda	0.5	0.4		
Ghana*	1.1	1.4	3.6	4.4
Nigeria	2.0	1.5		
Burkina Faso	2.7	6.4		
Senegal	5.4	10.9		
Benin	7.3	11.6		
Rwanda	8.9	2.8	40.5	12.7
Togo	11.8	13.1		

Source: FinScope Surveys, 2016-2020; IMF Financial Access Survey, 2022

*Data from 2018

[40] Osusus are communal thrift associations into which members contribute a set sum of money each week that is then allocated to one person. This is then repeated until each member collects.
[41] Teklas are more formal collective savings associations, where participants save towards a common agenda. Unlike osusus, teklas do not allocate money to one individual.

73. Low financial inclusion is driven by low income, low trust in financial institutions, lack of necessary documentations, high costs, and long distances to financial institution branches. Both demand and supply-side factors contribute to low levels of account access. While low incomes are the result of the country's fragility and low economic growth, factors such as low trust are associated with lack of financial literacy and "fear" factors that individuals have in using financial services. High costs for financial services point to limited competition as well as a fee driven model for payment services. While regulated financial institutions are permitted to practice agent banking in accordance with the relevant regulations, long distances to financial institutions' branches point to limited investment in outreach infrastructure particularly in rural areas. Geographic outreach indicators in Figure 2, however, show that the Gambia compares well against peer countries. Lastly, the lack of necessary documentation to open a transaction account points to the need for a simplified and tiered approach to know-your-customer (KYC) procedures, as well as the introduction of a "basic" bank account product for vulnerable communities (e.g., rural communities, youth, those with low income). Introducing a simplified KYC approach and basic bank accounts will require amendments to the legal and regulatory frameworks of banks and NBFIs, in addition to close coordination with financial institutions to ensure the ability to provide these products.

74. The Gambia launched a NFIS in January 2022 to chart a clear and coordinated roadmap toward achieving national financial inclusion goals. The operationalization of the NFIS will be essential for the country to achieve its financial inclusion goals. The NFIS identifies strategic enablers and pillars and puts forward ambitious targets to be achieved by 2025, as well as allocates responsibilities across different stakeholders in the public and private sector. The Strategy identifies demand side drive, supply side drive and regulatory driven bottlenecks to financial inclusion in the Gambia and includes a series of recommendations on how to address those bottlenecks. International experience indicates that implementation more effective if the responsible taskforce is converted into a formal body such as a National Financial Inclusion Committee or a National Payments Committee with a mandate beyond the expiration of the current NFIS. This formal entity should have the oversight powers to ensure that critical elements needed to progress and monitor implementation are in place, notedly: i) adequate institutional strength and capacity; ii) high-level political commitment; and iii) close coordination and cooperation with various relevant stakeholders (both private and public).

V. PAYMENT SYSTEMS AND DEVELOPING DIGITAL PAYMENTS

75. **Digital payments are the entry point for digital financial services (DFS), which play a critical role in the development and growth of the digital economy.** Research has shown many potential development benefits from financial inclusion, especially from the use of digital financial services, including basic transactional accounts like mobile money services or payment cards.[42] Global evidence suggests that digital payments are helping to accelerate digital financial inclusion.[43] Digital financial inclusion promotes efficient interconnection among participants in economic activities.[44] Shifting cash into digital accounts for government payments, remittances, micro, small and medium enterprise (MSME) payments, and agricultural value-chain payments can enable broad-based participation in digital economy. Both, access to and usage of transaction accounts as well as associated digital instruments and services are vital components of financial inclusion. For Gambia, increasing both access to and usage of transaction accounts as well as digital payment instruments and services are critical to promoting a digital economy. In addition, the COVID-19 pandemic and ensuing public emergency containment requirements highlighted the importance of developing DFS in Gambia.

76. **The low access to transaction accounts has also contributed to low usage of digital payments.** As data from FinScope shows, the main reasons Gambians use accounts include initiating/receiving payment and remittances. Other services such as savings, credit and insurance follow. Cash and cheques are the predominant payment instruments in Gambia, while the use of digital payment instruments such as debit cards, credit cards, credit transfer, direct debit, mobile money, is limited. On the contrary, physical cash and cheques dominate retail payments, particularly by businesses and some of the government agencies, on the collection side. According to the NFIS and FinScope, only 5 percent of adults use banking related products (including digital payment instruments) and only 2 percent of the adults use mobile money. The Gambia lags behind low-income group average whereas the percentage of those that made or received a digital payment was at 23 percent while for Sub-Saharan Africa at 31 percent.

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42 Demirgüç-Kunt, A., L. Klapper, D. Singer, S. Ansar, and J. Hess. 2018. "The Global Findex Database 2017: Measuring Financial Inclusion and the Fintech Revolution". Washington, DC: World Bank. doi:10.1596/978-1-4648-1259-0.

43 G20 World Bank Report, "The impact of COVID-19 on digital financial inclusion", November 2021

44 Dara, N. R. 2018. "The Global Digital Financial Service: A Critical Review to Achieve for Digital Economy in Emerging Markets." International Research Journal of Human Resources and Social Sciences, 5(1): 141-163.

77. **Specifically, mobile money has a potential for growth in the Gambia, though, its uptake is still limited.** According to FinScope, about 68 percent of adults in the Gambia are aware of mobile money, but that number has not translated into uptake and usage so far. Only 2 percent of adults use mobile money in the Gambia. The Mobile Money Regulation, despite its limitations, has been operational since 2011, but currently there are only two mobile money providers in the country.

78. **A number of different factors, separately and combined, underpin the lack of innovative players in the market that primarily contributes to low digital payment usage.** These factors include: i) the legal/regulatory gaps and uncertainty about the "rules of the game" as mentioned in Section IV; ii) high fees, driven by the dominance of banks in the payments market as well as an asymmetric incentive structure (particularly in the payment cards market); iii) lack of modernization in the payments systems infrastructures; iv) lack of interoperability in digital payment instruments and access channels; v) continued use of paper-based payment instruments for government payment collections and disbursements; and vi) low levels of financial literacy.

79. **The legal and regulatory framework governing payments is drawn from several acts, regulations, and guidelines.** These acts include: i) the Banking Act (2009); ii) the Regulation of Mobile Money Services (2011); iii) the Consumer Protection Act (2014); iv) the Payment Systems Act (2016); v) the Non-Bank Financial Institutions Act (2016); vi) Non-Bank Financial Institution Rules and Guidelines on Policies and Procedures (2016); and vii) Anti-Money Laundering and Combating Terrorism Financing Guidelines. While some of the oversight aspects of payment infrastructure and payments service providers are covered in some of the aforementioned acts and regulations, the country does not have a stand-alone comprehensive oversight framework. Such a framework is encouraged to facilitate the assessment of risks that payment service and infrastructure providers can pose to the broader National Payments System.

80. **Gambia would benefit from updating its current Payment Systems Act, given new developments in the payments space over the last 5 years.** It is important to expand the payment service/infrastructure provider definition to include emerging business models, fintechs, and paytechs, such as payment initiators, payment gateways, and merchant aggregators. Amendments should cover the following aspects, among others: i) tokenization and the use of aliases to safeguard transaction data and account data; ii) payment system, instrument, channel and account interoperability; iii) fair, transparent and risk-based criteria for direct membership in payment systems; iv) comprehensive oversight; and v) financial literacy as a policy objective.

81. Similar updates should be considered for the mobile money regulation. The CBG should consider reframing the regulation in order to cover e-money more broadly. This change would pave the way the licensing of companies that provide other e-money services (beyond mobile money) such as online money and prepaid cards.

82. The Gambian payments market is dominated by commercial banks, which act as both issuers and acquirers. Other actors in the market, including NBFIs, money transfer operators (MTOs), and MMOs, play a diminished role. In terms of payment systems infrastructure, the central bank operates a real time gross settlement (RTGS) system (large value payment system that settles credit transfers), a securities settlement system (SSS), as well as an automated clearing house (ACH) which clears checks, credit transfers and direct debits (of DAL 100,000 or less). Moreover, there is a domestic card switch (GAMSwitch), which processes domestically issued debit/credit cards and is co-owned by the central bank and the private sector.

83. NBFIs and other actors in the market could play a critical role in the growth of the digital payments ecosystem of Gambia. FCs, for instance, have the capacity to reach remote areas and therefore can contribute to increasing transaction account access. However, these entities will need to further integrate with underlying payment systems and to incorporate more digital channels to increase usage. Specifically, allowing FCs to become direct members to the ACH would decrease their dependence on banks and would open more digital channels to directly connect to other financial institutions, lowering costs to their customers. Although, MMOs are gaining traction in the country, but they remain at a nascent stage. Opening up the ACH to MMOs can increase transaction account interoperability by facilitating the seamless movement of funds between different types of transaction accounts in various financial institutions. Such services would go a long way to growing the uptake and usage of mobile money. Meanwhile, under the current regulatory regime, paying out international remittances through mobile wallets is not permitted. So, digitalizing MTO channels presents a good opportunity to drive access and usage of digital payments. In this context, Gambia Revenue Authority (GRA) could also consider becoming a direct participant to the ACH as it already has a settlement account with the central bank.

84. All payment systems infrastructure would benefit from upgrades in order to adequately support an increased number of direct participants. In addition to upgrading the ACH system, the CBG should consider modernizing the RTGS system. Similarly, the capabilities of GAMSwitch should be enhanced to enable the processing of internationally issued cards as only domestically issued cards are processed at present.

85. The digitization of government payments can further drive the shift away from cash and checks in Gambia. Currently, disbursements of government payments such as public sector salaries, pensions, and some social assistance transfers are channeled through transaction accounts, but government payments to vendors are still done in checks. Moreover, on the collection side, cash and checks are still frequently used. Encouraging the collection of government payments through payment aggregators can relieve some of the administrative and cost burden that individual government agencies face by collecting payments in their physical premises. To this end, the Treasury should encourage the government agencies to expand and/or establish agreements with third party payment aggregators to collect on government receivables.

86. Promoting the development of the electronics payments acceptance infrastructure can further incentivize the use of digital payments. ATM coverage compares well against peer countries with about 8.6 ATMs per 100,000 adults in 2020 (Figure 2). Most ATM transactions are cash-out even though electronic payments from ATMs to utilities and a few other merchants are growing. As of June 2019, there were only about 135 point-of-service (POS) terminals installed in merchants for accepting card payments around the country, with most of them concentrated in the Banjul area (primarily those frequented by tourists). The fees linked to POS devices as well as their cost are perceived to be high and prohibitive by merchants. Connectivity issues further exacerbate the usage of the limited acceptance infrastructure and further discourage uptake of card payments. More cost-effective POS terminals could be promoted to help lower costs faced by merchants, while subsidized solar or mobile devices can be considered to address internet connectivity and electricity issues. Only one bank and one MNO have deployed light electronic payments infrastructure (i.e., QR codes), which is lower cost and easier to use than traditional POS terminals. The CBG and GAMSwitch can work together the private sector to address this issue.[45]

87. Financial literacy is an important lever to further advance financial inclusion and usage of digital payments in the Gambia. According to FinScope, two of the main reasons cited for not having a transaction account include the lack of trust in financial institutions as well as lack of knowledge on how to open/operate one. The results make the need for awareness imminent in the Gambia. However, in order to obtain a better and deeper understanding of the financial literacy levels and main drivers, CBG and other national authorities could consider conducting a baseline financial literacy survey at a nationally representative level. The findings could inform targeted interventions by CBG, and other public and private sector stakeholders in the digital financial services market.

[45] In Ghana, for instance, the Central Bank's payment systems entity (GhIPSS) was instrumental in selecting and developing a supporting structure to roll out MPOS devices to drive the acceptance of digital payments.

88. **Further, the implementation of a National Financial Education Strategy (NFES), focusing on DFS, is necessary to expand the development and usage of these services.** FinScope data finds that the main barriers to using mobile money are related to lack of information and education on the service. A recent randomized study on mobile money in The Gambia also found evidence that low adoption and usage of these services is linked to a lack of information on the platform at large.[46] Low literacy (only 51 percent of adults are literate) and education levels (77 percent of adult population have primary school education or less – Finscope) further exacerbate issues of awareness and complicate DFS promotion initiatives. A NFES developed along with the Ministry of Basic and Secondary Education (MoBSE) would anchor this learning in education curricula, going beyond the National Financial Literacy Scheme planned by the NFIS. A DFS specific component within such a strategy will be critical to increase demand while addressing specific "fear" factors that individuals and merchants have in using these services, e.g., perception of lack of soundproof of payment if paper is not used; fear that the new modalities may be vulnerable to fraud; fear of dealing with unresponsive, complicated systems prone to operational error; and perception of loss of privacy.

VI. ROLE OF THE STATE IN DEVELOPING LONG-TERM FINANCE

A. Preconditions for Capital Market Development

89. **Certain preconditions need to be in place for capital markets development to be possible, and the authorities should consider developing comprehensive policies and strategies aimed at fulfilling these preconditions.** Research and experience with capital market development[47] has identified a series of preconditions that can be grouped as follows: i) macro-fundamental including macro-political and fiscal stability, level of savings, and the level of interest rates; ii) the broader legal and regulatory framework including insolvency law, tax law, and securities markets regulations; and iii) financial sector development including banking sector soundness. Without these basic preconditions, it is extremely difficult to build deep, liquid, and orderly securities markets in the short and medium term. A macroeconomic environment characterized by a fragile recovery from the pandemic, fiscal risks and debt vulnerabilities and a legacy of political tension, institutional fragility

[46] Cruces, G., H. Jawara, A. Touray, F. Singhateh. 2020. "Information, Price, and Barriers to Adoption and Usage of Mobile Money Evidence from a Field Experiment in the Gambia" Partnership for Economic Policy Working Paper No. 2020-17
[47] Capital Markets Development: Causes, Effects, and Sequencing, World Bank, December 2019

and weak governance are all factors present that may hinder Gambia's ambition to develop a capital market.

90. The government debt market is characterized by a small and underdeveloped primary market, narrow and undiversified investor base, no liability management operations, and no secondary market trading. The government of the Gambia issues domestic debt through the CBG on a weekly basis through an auction system on the primary market. Although the domestic yield curve has been extended to 30 years, issuance is concentrated at the short and long end of the yield curve with few issuances of medium tenor. Main holders of government debt include commercial banks (53 percent), other non-banks (25 percent) – the majority of which is held by the SSHFC, and the CBG (22 percent). Retail investors and nonresident investors do not appear to participate in the government debt market. The debt management office has not engaged in any liability management operations such as buy-backs or switch auctions but intends to reduce the share of short-term maturing instruments (T-bills and SAS) while increasing the share of longer-term debt instruments to mitigate refinancing risks. There is currently no secondary market trading of government bonds, however there are plans to develop one.

91. A benchmark building strategy can help to prioritize and sequence policy actions needed to support government debt market development. This strategy should focus on liability management operations, building a secondary market, and diversification of the investor base on order to deepen and consolidate the yield curve, especially medium-term bonds.

92. MoFEA has a medium-term debt management strategy in place, but more granular information on market development and borrowing plans is advisable to enhance communication with government debt market participants. The debt management strategy covers a five-year period between 2021 and 2025 and sets out two main objectives: (i) ensure that the government's financing needs are met at the least possible cost, consistent with a prudent degree of risk, and (ii) promote domestic debt market development and provide efficient, transparent, and accountable debt management processes to mitigate operational and portfolio risks. Based on international good practices, the debt management strategy could provide more details on directions for government bond market development and lays out the annual borrowing plan with guidelines for the instruments, sizes, breakdown of the issuance between the instruments, type of transactions and frequency, and the regularity of domestic market operations. The strategy could discuss how the choice of instrument depends on investor's demand and provide explicit link to economic policy and environment.

93. The debt management directorate also needs to be strengthened. This MoFEA department is under-resourced in terms of the number of its staff and their level of expertise. Further, the directorate has limited access to data and communication with the market.

B. Social Security and Housing Finance Corporation

94. Several analyses have all concluded that there is an urgent need for major restructuring of SSHFC. These have begun with the Bank's 2015 State-Owned Enterprises (SOEs) Policy Note, the Bank Actuarial Review of the Federated Pension Scheme, an administrative review/HR audit commissioned by SSHFC management, and several analyses of the SOE cross arrears. An analysis of the accessible financial statements shows a downward trend in the corporation's income and profitability that may place the viability of the country's social security system at serious risk unless structural issues are addressed.

95. Focusing on the governance arrangements of SSHFC appears to be critical and opportune to ensure that structural reforms can land within the perimeters of an efficient corporate structure. Effective corporate governance is critical to the proper functioning of the financial sector and the economy. Financial institutions perform a crucial role in the economy by intermediating funds from savers and depositors to activities that support enterprise and help drive economic growth. Safety and soundness are key to financial stability, and the manner in which financial institutions conduct their business, therefore, is central to economic health. Governance weaknesses can result in the transmission of problems across the financial sector and the economy as a whole.

96. The Constituting Act of SSHFC sets the SSHFC governance standards and appears to lag behind good governance practices. Currently, the board is highly politicized and composed of seven members, including management, Ministry Secretary of the MOFA (or alternate), Ministry Secretary of Lands (or alternate), and representatives from stakeholder associations (pensioners, employees). Chairman and CEO are appointed by the President of the country. No particular fit-and-proper requirements are to be met, and against this backdrop, roles and responsibilities among Government, board, and management ultimately overlap and blur. The government is planning to reform the current set up suggesting assigning CEO appointment to the board, to introduce competence standards for the selection of perspective board candidates, and to set up board committees to support the workings of the board.

97. The governance arrangements for SOEs will likely undergo important changes that will enhance current practices. The new SOE bill is long overdue and is being finalized by the Ministry of Justice to ensure consistency with the constitutional principles that The Gambia has embraced, before submitting for parliamentary approval. It will repeal the 1990 Public Enterprise Act and will represent an important step in the right direction of reform. This is an additional milestone that contributes to a reform process for SOEs that has initiated almost a decade ago with among other things the amendments to several SOE acts and the creation of a code of corporate governance for SOEs, a set of standard practices to adopt at company level.

98. The draft SOE Bill will have impacts on the constituting Act of the SSHFC. The SOE Bill introduces an SOE oversight Commission, appointment procedures for board and management, board composition expectations in terms of professionalism and objectivity, internal controls guidance, dividend policy for the State, and transparency and disclosure enhanced practices. It also identifies prohibitions, such as multiple directorships, and defines conflict of interest processes. If passed, the SSHFC constituting Act will have to be revised to ensure consistency with the new Framework Act. Overall, the best-case scenarios that have provided evidence that works well for SOEs have subjected SOEs to Companies Act norms and procedures, and this could still be considered in the process of corporate transformation and restructuring, as this has already been the case for six SOEs.

99. Monitoring performance of SSHFC remains challenging. The Corporation has not published financial statements since 2018, and it does not seem to be in the habit of signing performance contracts with the government. Internal control functions (audit, compliance, and controls) have been on the reform radar for long time, along with the need to create a risk function to administer the funds and housing finance loans. Audit and Risk Committee at the board level are not yet present as well.

100. Lack of regulatory authority and back logs in the workings of the oversight parliamentary committees represent structural deficiencies that warrant attention. While the SSHFC has the mandate to demand that contributions are paid on time and to impose sanctions for delays, it does not report to any regulator. As mentioned earlier, there is no pension regulator, and the housing finance arm is not under the banking regulator purview. According to the constitution, the ultimate responsibility for the public accounts lies with the National Audit Office (NAO), which reports its findings to the National Assembly Public Enterprise Committee (PEC). However, the backlog at the PEC prevents timely actions and/or investigations, which is problematic. MoFEA and NAO has excused past due contributions as well as audits, and an audit for the period between 2010 and 2017 was completed by a third-party international audit firm. NAO is responsible for following up on the audit findings. However, a regulator type agency may by best placed to follow up some of the recommendations.

101. The Role of the MoF in monitoring SOEs has also been enhanced with the creation of a dedicated SOE directorate. The institutional arrangements for SOE oversight have recently evolved towards a more centralized oversight set up, where the MoF plays a leading role. The SOE Directorate became operational in 2021, and it will in an effort to detect risks ramifications that the SOE portfolio can generate, centralize the oversight of the 11 SOEs, centralize information, and share via an already active portal.

102. SSHFC has taken action to ensure that reforms take place. The new SSHFC three-year restructuring plan has been embraced into the strategic plan that begins in 2022. The plan is comprehensive and contains important actions on how to reform operations, processes, controls, and governance of the corporation.

103. The SSHFC restructuring plan, to be effective, will have to be grounded on three main objectives: clarifying segregation of duties and responsibilities through the institution and among the business lines, ensuring better controls with creation of a risk oversight function, and adopting better disclosure practices. Internal controls, including audit risk and compliance, will have to be re-designed, made independent and resourced. An ERM will have to be designed and implemented and resourced as well. External communication via disclosure of financial information, audit reports, quarterly financials, will have to be re-activated as well to ensure better scrutiny and oversight of SSHFC operations.

ANNEX 1: FINANCIAL SECTOR STRUCTURE

	As of December 2021			
	Number of Institutions	Assets (millions of GMD)	Percent of Total Assets	Percent of GDP
Commercial Banks	**12**	**76,241**	**86.2%**	**73.5%**
Other deposit taking financial institutions	**126**	**4,786**	**5.4%**	**4.6%**
Finance Companies	3	2,393	2.7%	2.3%
Credit Unions	54	2,383	2.7%	2.3%
VISACAs[1/]	69	10	0.0%	0.0%
Other Finance Corporations				
Pension funds	**2**	**5,325**	**6.0%**	**5.1%**
Federated Pension Scheme (FPS)[2/]	1	2,366	2.7%	2.3%
National Provident Fund (NPF) [2/]	1	2,958	3.3%	2.9%
Insurance Corporations	**11**	**1,186**	**1.3%**	**1.1%**
Life Insurance	2	215	0.2%	0.2%
Non-life Insurance	9	651	0.7%	0.6%
Industrial Injuries Compensation Fund (IICF) [2/]	1	320	0.4%	0.3%
Other Finance Intermediaries	**1**	**605**	**0.7%**	**0.6%**
Housing Finance Fund[2/]	1	605	0.7%	0.6%
Financial auxiliaries	**156**	**347**	**0.4%**	**0.3%**
Foreign Exchange Bureaus[3/]	156	347	0.4%	0.3%
Money transfer organizations				
Social Security and Housing Corporation[4/]	**1**	**6,249**	**7.0%**	**6.0%**
Total	**309**	**88,490**	**100%**	**85.3%**
Memorandum Item				
Nominal GDP		103,700		

Source: CBG; IMF, World Economic Outlook; WB FSAP team estimates and calculations.

Notes:

1/ Figures for Village Savings and Credit Associations (VISACAs) are as of December 2017

2/ Figures for Pension Funds, Insurance Fund, and Housing Finance Fund are as of December 2019.

3/ Figures for Foreign Exchange Bureaus are as of December 2020.

4/ The SSHFC is comprised of assets from: i) the Federated Pension Scheme (FPS); ii) the National Provident Fund (NPF); iii) the Industrial Injuries Compensation Fund (IICF), and iv) the Housing Finance Fund (HFF).

ANNEX 2: FINANCIAL SOUNDNESS INDICATORS

	2018	2019	2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021
Capital adequacy							
Capital Adequacy Ratio	31.68%	31.37%	32.56%	31.76%	28.31%	27.28%	29.01%
Regulatory Capital Ratio (i.e., T1+T2)	33.03%	32.65%	33.74%	32.89%	29.50%	28.53%	30.64%
Primary Capital Ratio (i.e., T1)	30.28%	30.09%	31.10%	30.37%	26.87%	26.03%	27.26%
Asset composition (Figures are in thousands of GMD)							
Agriculture, Forestry, Fishing and Hunting	93,849	144,768	278,571	266,588	208,570	33,020	26,292
Community, Social and Personal Services	868,808	1,986,035	1,000,588	1,048,727	1,151,303	1,539,966	1,817,604
Construction							
Electricity, Gas, Water and Energy							
Manufacturing	23,463	90,835	71,652	30,555	35,112	42,970	97,448
Mining And Quarrying							
Real Estate	1,091,080	1,454,526	2,041,422	2,295,608	2,385,343	2,474,425	3,074,313
Restaurants And Hotels	595,825	408,483	416,001	330,679	315,342	332,842	315,981
Transport, Storage and Communications	427,123	663,171	565,017	524,539	432,409	407,329	308,899
Wholesale And Retail Trade	1,726,604	1,684,937	1,733,582	1,711,711	1,604,352	1,667,563	1,957,367
Other financial intermediaries	178,531	356,900	190,284	208,909	178,807	187,424	263,974
Other Sectors	534,621	560,675	1,105,119	1,209,783	1,532,909	1,388,938	1,495,626
Asset quality							
Non-performing loans (NPL) as percent of gross loans	3.15	4.55	6.82	7.74	5.53	5.64	5.15
Restructured loans as percent of total loans	0.40%	1.72%	1.81%	1.43%	1.14%	0.86%	1.43%
Non-accrual loan ratio	2.76%	2.82%	4.63%	6.31%	4.46%	4.78%	3.72%
Provisions + write-offs as percent of NPL	93.07%	59.52%	62.41%	42.18%	66.49%	64.35%	58.49%
Loan Loss Reserve Ratio	2.93%	2.71%	4.02%	3.26%	3.74%	3.63%	3.01%
Loan loss provision to NPL	93.07%	59.52%	62.41%	42.18%	66.49%	64.35%	58.49%
Loan loss provision to gross loans	2.93%	2.71%	4.02%	3.26%	3.74%	3.74%	3.01%
Earnings and profitability							
ROA (%)	2.72	3.14	3.16	3.09	2.83	2.66	2.49
ROE (%)	16.69	20.82	22.47	23.35	21.97	21.20	19.87
Net interest margin	6.76%	6.47%	6.55%	5.94%	5.70%	5.53%	5.36%
Gross income as percent of average assets	8.70%	8.30%	8.12%	7.56%	6.70%	7.23%	7.24%
Overhead Ratio	69.39%	54.35%	51.36%	50.48%	58.74%	71.24%	52.42%
Number of employees	1635	1758	1927	1856	1860	1803	
Number of branches	87	86	86	86	88	88	88
Liquidity							
Liquid assets as percent of total assets	69.24	70.15	72.37	71.57	72.39	70.65	70.01%
Liquid assets as percent of short-term liabilities	94.75	91.60	93.53	92.83	91.95	89.58	92.03%
Foreign currency liabilities as percent of total liabilities	26.92%	28.49%	30.84%	30.54%	27.17%	27.85%	37.31%

Source: CBG

ANNEX 3: IMF FINANCIAL SECTOR STABLITY REVIEW (FSSR)

The IMF Financial Sector Stability Review (FSSR) was a key building block for the assessments summarized in Section III. Between end-October to mid-November 2019, the IMF conducted a FSSR review, covering the following areas: (i) banking regulation and supervision; (ii) stress-testing capacity; (iii) systemic risks and macroprudential policies; (iv) bank crisis preparedness and management, resolution planning and safety nets; (v) financial inclusion and stability; and (vi) financial statistics. During the FSAP scoping note review in July 2020, it was agreed that the FSAP would provide an assessment of the banking sector given an estimated severe impact of the pandemic on the Gambia. In November 2021 during the FSAP's technical mission, the team decided to develop a separate technical note on this assessment given the wealth of information and data available 2 years after the FSSR. All findings summarized in this FSA were developed with the FSSR key findings and recommendations (summarized below) in mind.

The FSSR identified several emerging macro- and microfinancial vulnerabilities, but the lack of data prevented a more comprehensive analysis. After an extended period of sluggish lending, some banks may struggle to adopt basic underwriting and credit risk-management standards. Currency mismatches on banks' balance sheets pose vulnerabilities, while the lack of comprehensive supervisory data on foreign exchange loans impedes proper monitoring. Strong balance sheet linkages between banks and nonbanks, particularly pension funds, also highlight potential sources of vulnerability.

The changing macroeconomic environment and rapid credit growth call for prompt development of a comprehensive macroprudential framework. Data collection should be strengthened to allow thorough monitoring of emerging risks. The macroprudential authority should be assigned formally to the CBG. A macroprudential framework should be developed and include a clear mandate, well-defined objectives, a set of instruments, adequate powers, and strong accountability.

The CBG has received numerous technical assistance (TA) missions in recent years from multinational institutions, including from the IMF/MCM. There has been some progress in modernizing monetary policy and systemic liquidity management, but the integration of the TA recommendations for financial sector oversight and stress testing has been slow. In the mission's view, there is a need for an overhaul in the processes for absorbing TA in general, leaving more time to analyze and implement the recommendations. It is recommended to place a resident banking supervision advisor with the CBG.

In banking supervision, important gaps remain before the risk-based supervision framework can be implemented. Some basic supervisory functions, such as data quality and offsite monitoring and analysis, are either inoperative or inefficient, and the capacity to understand and evaluate the risks in the banking system needs significant strengthening. A range of risks (e.g., market and operational) are not defined in the regulatory framework and the CBG has little information on them.

The banking sector regulatory framework should be urgently revised and core skills in supervision should be reinforced. The Banking Act lacks important definitions for issuing prudential requirements and does not fully identify regulatory tools. Regulations should be enhanced and include basic minimum requirements, reflecting international standards according to the principle of proportionality. The assignment of clear responsibilities for specialized functions in the Financial Supervision Department (FSD) is essential to properly enforce minimum requirements.

There is a need to strengthen the CBG's capacity for the early detection of emerging stress in banks. Early intervention is essential to incorporate early-stage preventive actions well before any breach of prudential requirements occurs. The CBG should also develop contingency plans, setting out preventive and corrective actions pertinent to a range of bank-stress scenarios.

The CBG supervision and regulatory functions are severely understaffed and the modest expansion plans in the FSD staffing may not address these shortages. Understaffing issues are compounded by highly manual data management processes. This leaves little room for forward-looking thinking, introducing state-of-the-art methodologies, and updating processes across all the areas—including those recommended by previous TA missions. As all of these changes in banking supervision would imply significant changes in the supervisory processes, it is recommended to place a resident banking supervision advisor with the CBG.

A diagnostic was undertaken of the past TA, current stress testing capabilities, and key vulnerabilities for which the stress testing should be designed. The work on stress testing had dwindled after the previous TA missions had left and, at present, the CBG is not undertaking any stress testing. The reasons for discontinuation appear to be lack of purpose, lack of depth of understanding, lack of confidence in running the tests, lack of resourcing due to competing tasks, highly manual and error-prone process for data gathering, and movement of people with stress testing knowledge. To build capacity in stress testing, there is a need for commitment, including from senior management. It can be achieved by making senior management more aware of the broader day-to-day value of the end-to-end stress testing process, coupled with a high-level governance framework.

The mission was concerned about the poor financial sector data quality at the CBG. Although the data gathering process began four months before the mission, the data continued to arrive in various states of refinement over the course of the mission. Five corrected versions of the data were provided, with the last arriving toward the very end of the mission, as the earlier versions contained errors or inconsistencies. These reflect the highly manual data handling by the CBG.

The CBG is the resolution authority for banks but has limited legal powers for effective resolution. The BA contains some of the legal powers needed but is overly dependent on court approval. The CBG should develop a draft bill to amend the BA to incorporate resolution powers broadly aligned to those recommended in the Financial Stability Board (FSB) *Key Attributes* but modified to be suitable for The Gambia. It is also necessary to develop policies and processes for how the CBG would seek to resolve a bank. Guidance on bank resolution should be developed. Deposit insurance should be established once the preconditions for it have been met. Cross-border coordination for bank recovery and resolution is essential, given the dominance of foreign-owned banks. Emergency liquidity assistance policies and collateral arrangements should be developed.

A wide variety of large and small nonbank financial institutions (NBFIs) provide access to financial services in The Gambia. Supervising the diverse array of provider types requires a balanced approach that ensures these entities are able to serve their customers without taking undue risk. The CBG needs a more proportionate regulatory and supervisory approach to deposit-taking NBFIs based on their individual risk profiles. This is particularly important for the largest finance company, which has deposits exceeding that of three commercial banks. The NBFI sector would also benefit from updated or streamlined regulations, and greater legal clarity regarding its oversight of credit unions.

The supervision program for smaller deposit taking NBFIs and mobile money providers should be more risk focused. Although the mobile money sector is still nascent, the CBG would benefit from having a sound yet flexible regime in place to facilitate innovation and responsible growth. Digital financial services will likely play an important role in the forthcoming National Financial Inclusion Strategy; so, capacity building in this area will be essential for the success of this effort.