Bank Of Zambia

Bank of Zambia Monetary Policy Statement

JAN - JUN 2014

Bank of Zambia

MISSION STATEMENT

The principal purpose of the Bank of Zambia is to achieve and maintain price and financial system stability for balanced macro-economic development.

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Executive Summary

This statement presents the economic outlook for 2014 and then reviews the monetary policy outcome during the second half of 2013.

Global growth is projected to rise to 3.7% in 2014, driven by stronger demand in the United States. Further, the Euro Area is expected to pull out of recession, while growth in emerging markets and developing economies is expected to rise slightly supported by domestic demand, recovering exports and supportive fiscal, monetary and financial conditions.

Downside risks to the forecast include weaker growth in major emerging markets due to structural bottlenecks in infrastructure, labour markets and investments. Further expectations of a turning point in US quantitative easing has led to an increase in long-term yields in the US and other economies, posing financial risks of asset price overshooting or even balance of payments disruptions. The slower growth in China is likely to affect other economies, particularly commodity exporters in developing countries. Geopolitical risks, fragmented financial sector and high debt in euro area, as well as related fiscal and financial risks in other advanced economies including Japan and US could also affect global output.

On the domestic front Zambia's economic prospects for 2014 remain favourable. Growth will largely be driven by developments in the construction, manufacturing, agricultural, mining, energy and tourism sectors. The external sector is also projected to improve supported by continued growth of non-traditional exports, coupled with the expected recovery in the global economy.

The main risks to the economic outlook include:

- Adverse weather conditions coupled with high prices of agricultural inputs could negatively impact the agriculture sector;
- Slower growth in China may affect demand and the price of copper, Zambia's main export commodity; and
- Risk aversion by portfolio investors, in response to the Fed's tapering[1], could result in capital outflows, pressure on the exchange rate, inflation and lower growth.

During the first quarter of 2014, annual overall consumer price inflation is expected to increase marginally to an average of 7.2% from an average of 7.0% in the fourth quarter of 2013. This will be mainly as a result of high prices of various food items due to seasonal low supply coupled with cost-push pressures arising from the pass-through effects of the depreciation of the Kwacha exchange rate. However, during the second quarter of 2014, inflation is projected to trend downwards to 6.8% by end-June 2014. This forecast is premised on anticipated improvements in the supply of various food commodities.

In the two- year period ending 2015, monetary policy formulation and implementation will remain focussed on attaining Government's broad economic objectives, which include reducing inflation to 6.5% in 2014 and 5.0% by 2015; achieving real GDP growth rate of at least 7% in 2014 and 7.5% in 2015; limiting overall fiscal deficit to 6.6% of GDP in 2014 and 4.3% in 2015; limiting domestic borrowing to at most 2.5% of GDP in 2014 and 2.2% in 2015; and accumulating foreign reserves to over 3 months of import cover in 2014 and 4.0 months in 2015.

The Bank of Zambia will continue to monitor global and economic developments and use market based instruments in its conduct of monetary policy.

With regard to monetary policy outcome during the second half of 2013, monetary policy was focused at achieving the end-year inflation target of 6.0%. In this regard, monetary operations were aimed at maintaining the 5-day weighted average interbank rate within a corridor of +/- 200 basis points of the Bank of Zambia (BoZ) policy rate target, which was raised to 9.75% in July 2013 from 9.50% in June 2013, due to rising inflationary pressures. The Bank undertook aggressive open market operations to address high liquidity levels in the banking system and the 5-day moving average interbank rate remained within the corridor, closing at 10.2% compared with 11.3% at end-June 2013.

The performance of monetary policy during the second half of 2013 was generally favourable, as end year inflation at 7.1% was lower than the projected 7.5%, although 1.1 percentage points above the end-

[1]This refers to the United States Federal Open Market Committee's decision to reduce the size of its bond buying program known as Quantitative Easing (QE) that was designed to stimulate the economy, as it has served the secondary purpose of supporting financial market performance in recent years. The US Monetary Authority will reduce its monthly asset purchases by US$10 billion, as long as the US economy continues to improve, thus eventually ending the QE program by end 2014. Asset purchases were reduced to US$75 billion in January 2014 from US$85 billion, then to US$65 billion effective February 2014, and US $55 billion effective April 2014.

year target of 6%. This outturn reflected an increase in non-food inflation as food inflation slowed down during the review period.

Broad money (M3) edged up by 11.6% to K31,042.2 million as at end-December 2013 from K27,807.8 million at end-June 2013, reflecting an increase in commercial banks' foreign assets and net government spending.

Domestic credit rose by 8.6% during the second half of 2013 compared with an increase of 32.6% recorded in the first half of 2013. In absolute terms, domestic credit rose to K28,404.0 million in December 2013 from K26,164.7 million as at end-June 2013. This was largely on account of lending to government, which increased by 30.1% to K10,570.8 million, while credit to the private sector fell by 1.1% to K17,805.1 million.

In the Government securities market, both the weighted average Treasury bill yield rate and weighted average bond yield rate rose to 15.3% and 16.3% from 13.1% and 15.2%, respectively in the previous half of the year. Meanwhile the commercial banks average lending rate remained relatively unchanged at 16.4% in December 2013 compared with 16.3% registered in June 2013.

With regard to the foreign exchange market, the Kwacha was characterised by a depreciating trend against most major trade partner currencies except the rand. Firm domestic demand due to high kwacha liquidity, the steady recovery of US economy, austerity measures amid record unemployment levels in the Eurozone and economic slowdown in China contributed to the observed pressure on the Kwacha exchange rate. The decline in the price of copper and appreciation of the dollar globally also contributed to the weakening of the local currency.

Subsequently the real effective exchange rate (REER) index depreciated by 0.9% to 96.6 in December 2013 from 95.7 recorded in June 2013. Implying that exporters had a competitive edge compared to the first half of the year when the REER appreciation by 5.1%.

Preliminary data for the second half of 2013 show that Zambia's external sector performance was unfavourable, with the overall merchandise trade balance (c.i.f) recording a deficit of US $53.6 million compared with a surplus of US $385.6 million registered during the first half of the year. This was explained by the rise in **merchandise import bills** while merchandise export earnings declined.

In terms of fiscal performance, preliminary data indicate that the Central Government budget recorded a deficit of K3,192.9 million during the second half of 2013 against the programmed deficit of K4,806.0 million.

With regard to performance of the economic programme, preliminary data indicate that the Net Domestic Assets of the Bank of Zambia, the Net Domestic Financing of Government and the Unencumbered International Reserves quantitative performance criteria were off track as at end-December 2013.

1.0 Introduction

This Monetary Policy Statement provides an economic outlook and inflation projection for the first half of 2014. It also outlines the objectives and major challenges of monetary policy for the first half of 2014. The report closes with a review of the performance of monetary policy during the period July to December 2013.

2.0 Economic Outlook 2014

2.1 Global Economic Growth

Global economic growth is projected to rise to 3.6% from 3.0% in 2013, largely driven by recovery in advanced economies. Growth in the United States is projected to rise to 2.8% in 2014 from 1.9% in 2013 driven by higher domestic demand, supported in part by a reduction in the fiscal drag as a result of the recent budget agreement. The euro area is projected to strengthen growing by 1.0% in 2014, from -0.4% in 2013, led by the German and French economies. Activity in the United Kingdom has been buoyed by easier credit conditions and increased confidence, though economic slack will remain high, thus growth is projected at 2.4% up from 1.7% in 2013.

Growth in emerging and developing economies is expected to rise to 5.1% in 2014 from 4.7% in 2013, despite China's growth moderating to 7.5%, due to policy measures aimed at slowing credit expansion. Regional growth in Sub-Saharan Africa is expected to remain robust in the medium term, picking up from 5.1% in 2013 to 6.1% in 2014. The positive forecast is premised on increased investment in mining and natural resources paying dividends as well as rebound in global demand.

Downside risks to the global growth forecast include: The threat of lower than expected inflation in advanced economies, which increases real debt burdens and the premature increase in interest rates.

I. Corporate leverage has risen, accompanied in many emerging market economies by increased exposures to foreign currency liabilities. Asset valuations could come under pressure in several emerging markets, if interest rates rose more than expected and adversely affect investor sentiment;

ii. Financial market and capital market flows volatility remain a concern given the Fed will start tapering in 2014. Portfolio shifts and some capital outflows are likely with Fed tapering. When combined with domestic weakness, the result would be sharper capital outflows and exchange rate adjustments;

iii. The slower growth in China is likely to affect other economies, particularly commodity exporters in developing countries; and

iv. Geopolitical risks, fragmented financial sector and high debt in euro area, as well as related fiscal and financial risks in other advanced economies including Japan and US could also affect global output.

2.2 Zambia's Economic Outlook for the First Half of 2014

During the first half of 2014, Zambia's economic outlook remains positive. This is premised on the expected favourable developments in the agricultural and construction sectors as well as growth in government expenditure and significant foreign investment especially in the mining sector. The agriculture sector, which has shown resilience in recent years, is expected to benefit from the government's plans to improve resource allocation to the sector and planned investments in agriculture infrastructure and crop diversification. Growth in the construction industry is expected to gain from the continued increase in public infrastructure investments, including the Link Zambia 8,000 and other road networks, and energy projects. To this effect, domestic developments are expected to be in tandem with the projected annual Gross Domestic Product growth rate of 7%, while inflation is expected to slow down to 6.8% at end-June 2014 on account of the expected improved food supply in the latter part of the period.

Zambia's economic prospects are however subject to a number of risks. The country's dependence on the mining sector continues to expose the economy to external vulnerabilities, such as demand and price shocks. Further, with the global economy still plagued by uncertainty, demand for copper could remain depressed, even with China showing signs of recovery. This could adversely put a cap on a rally in copper prices, and consequently delay recovery of the mining industry, harming economic growth. In addition, downward risks to financial stability still persist as the emerging markets continue to be exposed to increased foreign currency liabilities.

3.0 Monetary Policy Objectives and Instruments for January - June 2014

Monetary policy during the first half of 2014 will continue to be focussed on achieving single digit annual inflation of 6.5%. Consistent with this objective, the Bank of Zambia will rely mainly on OMO and Government securities auctions to maintain the interbank rate within the BOZ policy rate corridor.

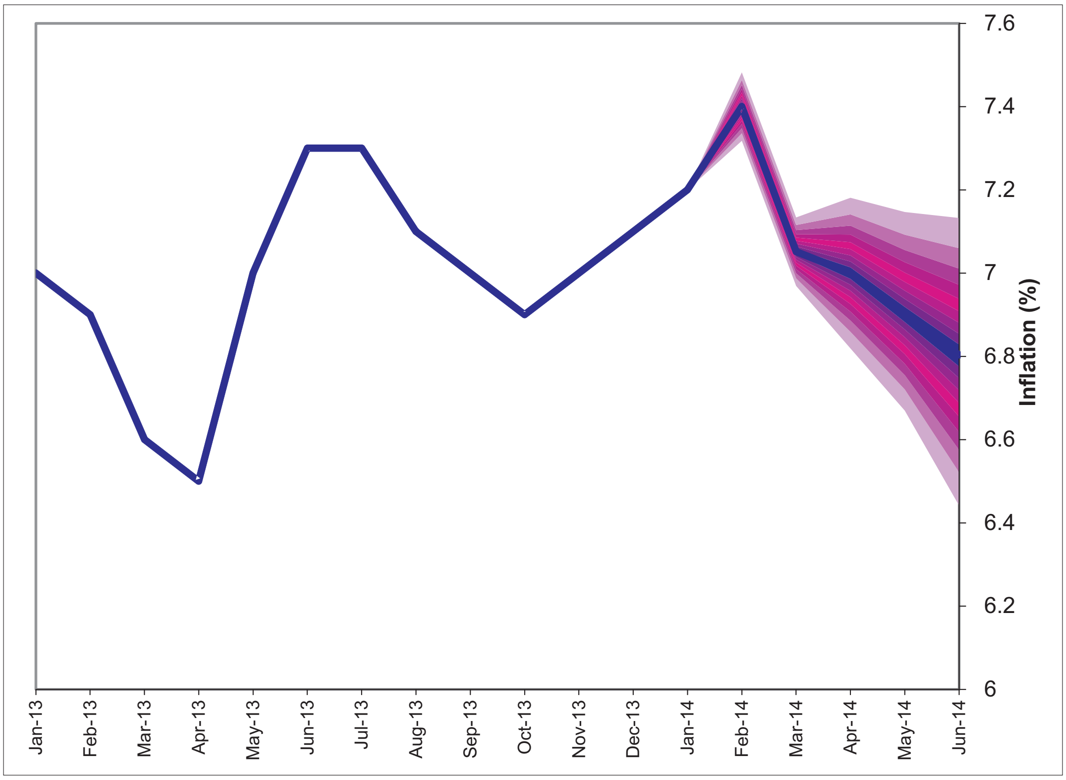
4.0 Inflation Projection for January - June 2014

During the first half of 2014, annual overall consumer price inflation is expected to slow down to 6.8% in June 2014 from the 7.1% recorded in December 2013 (see Chart 1 and Table 1).

Inflation is expected to increase marginally to an average of 7.2% in the first quarter of 2014 from an average of 7.0% in the fourth quarter of 2013. This outlook is premised on high prices of selected food items due to seasonal low supply. In addition, cost-push pressures may arise from pass-through effects of the depreciation of the exchange rate and the expected increase in water and electricity tariffs.

However, in the second quarter of 2014, inflation is expected to trend downwards to 6.8% at end-June 2014 while the average is projected to be around 6.9%. The downward trend is premised on anticipated improvement in the supply of food items as the harvest season commences and the fish ban is lifted.

Chart 1: Actual and Projected Inflation, January 2013 – June 2014



Source: Bank of Zambia

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Table 1: Actual Inflation and Projections, January 2012 – June 2014

Description		Projection (a)	Actual (b)	Forecast Error (b-a)
First Half	January	6.5	6.4	-0.1
of 2012	February	6.5	6.0	-0.5
	March	5.6	6.4	0.8
	April	6.1	6.5	0.4
	May	5.9	6.6	0.7
	June	6.5	6.7	0.2
	Average	**6.2**	**6.4**	**0.3**
Second Half	July	5.8	6.2	0.4
of 2012	August	6.4	6.4	0.0
	September	6.7	6.6	-0.1
	October	6.7	6.8	0.1
	November	6.8	6.9	0.1
	December	7.2	7.3	0.1
	Average	**6.6**	**6.7**	**0.1**
First Half	January	7.2	6.9	-0.1
of 2013	February	7.1	6.6	-0.3
	March	6.6	6.5	-0.5
	April	7.0	7.0	-0.1
	May	7.2	7.3	0.0
	June	7.2	7.3	-0.1
	Average	**7.1**	**6.9**	**(0.1)**
Second Half	July	6.8	7.3	0.5
of 2013	August	6.9	7.1	0.2
	September	7.4	7.0	-0.4
	October	7.3	6.9	-0.5
	November	7.4	7.0	-0.4
	December	7.2	7.1	-0.1
	Average	**7.2**	**7.1**	**(0.1)**
First half	January	7.2		
of 2014	February	7.4		
	March	7.1		
	April	7.0		
	May	6.9		
	June	6.8		
	Average	**7.1**		

Source: Bank of Zambia
Note: A positive number implies that actual inflation outturn was above the projection and the opposite is true

5.0 Monetary Policy Principles for the Period January 2014 - December 2015

In the two- year period ending 2015, monetary policy formulation and implementation will be geared towards attaining Government's broad economic objectives, which include:

i. Reducing inflation to 6.5% in 2014 and 5.0% by 2015;

ii. Achieving real GDP growth rate of at least 7% in 2014 and 7.5% in 2015;

iii. Limiting overall fiscal deficit to 6.6% of GDP in 2014 and 4.3% in 2015;

iv. Limiting domestic borrowing to at most 2.5% of GDP in 2014 and 2.2% in 2015; and

v. Accumulating foreign reserves to over 3 months of import cover in 2014 and 4.0 months in 2015.

The Bank of Zambia will continue to use market-based instruments in its conduct of monetary policy.

6.0 Conduct of Monetary Policy, July – December 2013

During the second half of 2013, monetary policy continued to be focused at achieving the end-year inflation target of 6.0%. In this regard monetary operations were aimed at maintaining the 5-day weighted average interbank rate within a corridor of +/- 200 basis points of the Bank of Zambia (BoZ) policy rate target. The Bank offered repos and term deposits through Open Market Operations (OMO) to steer the interbank rate towards the BoZ Policy Rate.

7.0 Challenges of Monetary Policy

During the review period, the implementation of monetary policy was faced with a number of challenges including the following:

i. Cost push pressures emanating from removal of fuel and maize subsidies in May 2013, which led to a 21% rise in fuel prices and translated into higher transportation and production costs and increased prices of maize products;

ii. Pass-through effects of the depreciation of the Kwacha against the US dollar; and

iii. Rise in liquidity levels of the banking system resulting from the 41.9% increase in civil service wages in September 2013.

Given these challenges, the Monetary Policy Committee decided to raise the BoZ Policy Rate by 0.25 percentage points to 9.75% in July 2013 from 9.50% in June 2013. Further, aggressive OMOs were undertaken to address high liquidity levels in the banking system (see Table 2).

Table 2: Selected Monetary Indicators, 2011 – 2013 (%)

	2011	2012	2013	
	Actual	Actual	Prog.	Actual
Overall Inflation	7.2	7.3	6.0	7.1
Non-food Inflation	10.2	6.1	3.2	8.2
Food Inflation	-3.9	8.4	2.8	6.2
BoZ Policy Rate (%)	n.a	9.25	n.a	9.75
Overnight Interbank Rate*	5.2	8.2	n.a	10.2
Reserve Money	6.3	53.0	-9.6	17.7
Broad Money	22.4	17.9	18.2	20.8
Domestic Credit	19.0	17.3	34.5	43.9
Government	-6.3	-37.7	144.8	218.8
Public Enterprises	70.8	602.6	-3.2	-66.0
Private Sector Credit	30.8	39.2	10.0	9.1
Domestic Financing (% of GDP)	2.5	2.3	1.5	4.7**

Source: Central Statistical Office - The Monthly; and Bank of Zambia

Notes: n.a - not applicable
-Indicates no target under the ECF Programme
- Inflation figures are on annual basis
*5-day moving average
**- preliminary

8.0 Assessment of Monetary Policy Outcome, July - December 2013

The performance of monetary policy during the second half of 2013 was generally favourable, as end year inflation at 7.1% was lower than the projected 7.5%, although 1.1 percentage points above the end-year target of 6%.

Money market liquidity rose during the second half of the year on account of net government spending and net purchases of foreign exchange by Bank of Zambia. However, these influences were partially offset by net sales of Government securities and net OMO withdrawals. The 5-day moving average interbank rate remained within the corridor and at end-December, closed at 10.2% compared with 11.3% at the end-June 2013. Nevertheless, reserve money increased by 17.7% to K8,164.5 million from K6,936.5 million in the first half of the year.

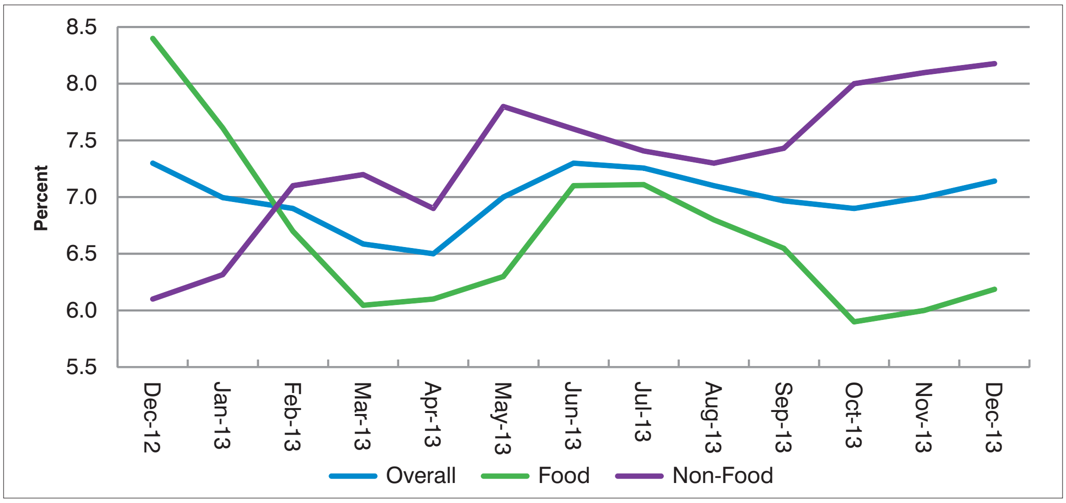
In the Government securities market, both the weighted average Treasury bill yield rate and weighted average bond yield rate for the six month period increased to 15.3% and 16.3% from 13.1% and 15.2% previously. Similarly, the commercial banks' average lending rate increased to 16.4% in December 2013 from 16.3% in June 2013.

With regard to the foreign exchange market, the Kwacha was characterised by a depreciation trend against most major trade partner currencies except the rand. This was attributed to both local and foreign influences. Firm domestic demand due to high Kwacha liquidity, the steady recovery of US economy, austerity measures amid record unemployment levels in the Eurozone and economic slowdown in China contributed to the observed pressure on the Kwacha exchange rate. The decline in the price of copper and the strengthening of the dollar globally also contributed to the weakening of the Kwacha.

8.1 Overall Inflation

Annual overall inflation slowed down to 7.1% in December 2013 from 7.3% in June 2013. The lower inflation outturn during this period was mainly credited to a decline in food inflation to 6.2% in December 2013 from 7.1% in June 2013. On the other hand, non-food inflation rose to 8.2% in December 2013 from 7.6% in June 2013 (see Chart 2 and Table 3).

Chart 2: Annual Inflation, Dec 2012 - Dec 2013



Source: Bank of Zambia

8.1.1 Non-Food Inflation

Annual non-food inflation remained generally high during the second half of 2013 rising to 8.2% in December 2013 from 7.6% in June 2013. This was attributed to higher inflation outturns for the following sub-groups: Transport, 13.7% [8.3%]; Restaurants and Hotels, 7.9% [6.4%]; Miscellaneous goods and services, 7.3% [6.8%]; Alcoholic Beverages, 6.8% [6.6%]; Furnishings and Household equipment, 6.3% [5.2%]; Recreation and Culture, 5.9% [3.4%] and Communications, 4.0% [2.8%].

The higher non-food inflation partly reflected pass-through effects of the relatively weaker Kwacha exchange rate coupled with effects of the 21% rise in fuel prices following the removal of the fuel subsidy. In addition, the high demand for various commodities during the Christmas period pushed prices of various commodities up.

8.1.2 Food Inflation

On the other hand, annual food inflation remained moderate in the second half of 2013, declining from a peak of 7.1% in June 2013 to 6.2% in December 2013. The fall in food inflation was explained by the steady supply of food items on the market, following the commencement of the marketing season for 2013. This was despite prices of mealie meal shooting up in the last two months of the year due to supply shortages of maize grain in some parts of the country.

Table 3: Inflation Outturn, Dec 2012 – Dec 2013 (%)

Period	Overall	Monthly		Year-to-date			Annual		
	1.1	Food	Non-Food	Overall	Food	Non-Food	Overall	Food	Non-Food
Jan-12	0.3	1.9	0.2	1.1	1.9	0.2	6.4	6.1	6.7
Feb-12	1.4	-0.1	0.7	1.4	1.8	0.9	6.0	5.5	6.5
Mar-12	0.7	1.9	1.1	2.8	3.7	2.0	6.4	6.4	6.4
Apr-12	0.4	0.5	0.7	3.5	4.2	2.7	6.5	6.4	6.5
May-12	0.0	0.3	0.6	3.9	4.6	3.3	6.6	6.8	6.3
Jun-12	0.7	-0.4	0.5	4.0	4.1	3.8	6.7	7.1	6.2
Jul-12	0.9	0.8	0.7	4.8	4.9	4.5	6.2	6.3	6.0
Aug-12	0.5	1.1	0.6	5.7	6.1	5.2	6.4	7.3	5.5
Sep-12	0.1	0.5	0.4	6.2	6.6	5.6	6.6	7.5	5.6
Oct-12	0.2	0.4	-0.3	6.3	7.0	5.3	6.8	8.2	5.4
Nov-12	0.8	0.2	0.1	6.4	7.3	5.5	6.9	8.0	5.8
Dec-12	0.8	1.0	0.6	7.3	8.4	6.1	7.3	8.4	6.1
Jan -13	0.2	1.1	0.5	0.8	1.1	0.5	7.0	7.6	6.3
Feb-13	1.2	-0.9	1.4	1.0	0.2	1.9	6.9	6.7	7.1
Mar -13	0.6	1.2	1.1	2.2	1.4	3.0	6.6	6.0	7.2
Apr-13	0.9	0.7	0.5	2.8	2.1	3.6	6.5	6.1	6.9
May-13	0.4	0.4	1.3	3.7	2.5	5.0	7.0	6.3	7.8
Jun-13	0.7	0.4	0.3	4.0	2.9	5.3	7.3	7.1	7.6
Jul-13	0.7	0.8	0.5	4.7	3.7	5.8	7.3	7.1	7.4
Aug-13	0.4	0.8	0.5	5.4	4.5	6.3	7.1	6.8	7.3
Sep-13	0.0	0.3	0.5	5.8	4.8	6.9	7.0	6.5	7.4
Oct-13	0.3	-0.3	0.2	5.8	4.5	7.2	6.9	5.9	8.0
Nov-13	0.9	0.3	0.3	6.1	4.9	7.5	7.0	6.0	8.1
Dec-13		1.2	0.6	7.1	6.2	8.2	7.1	6.2	8.2

Source: Bank of Zambia, Central Statistical Office Bulletin

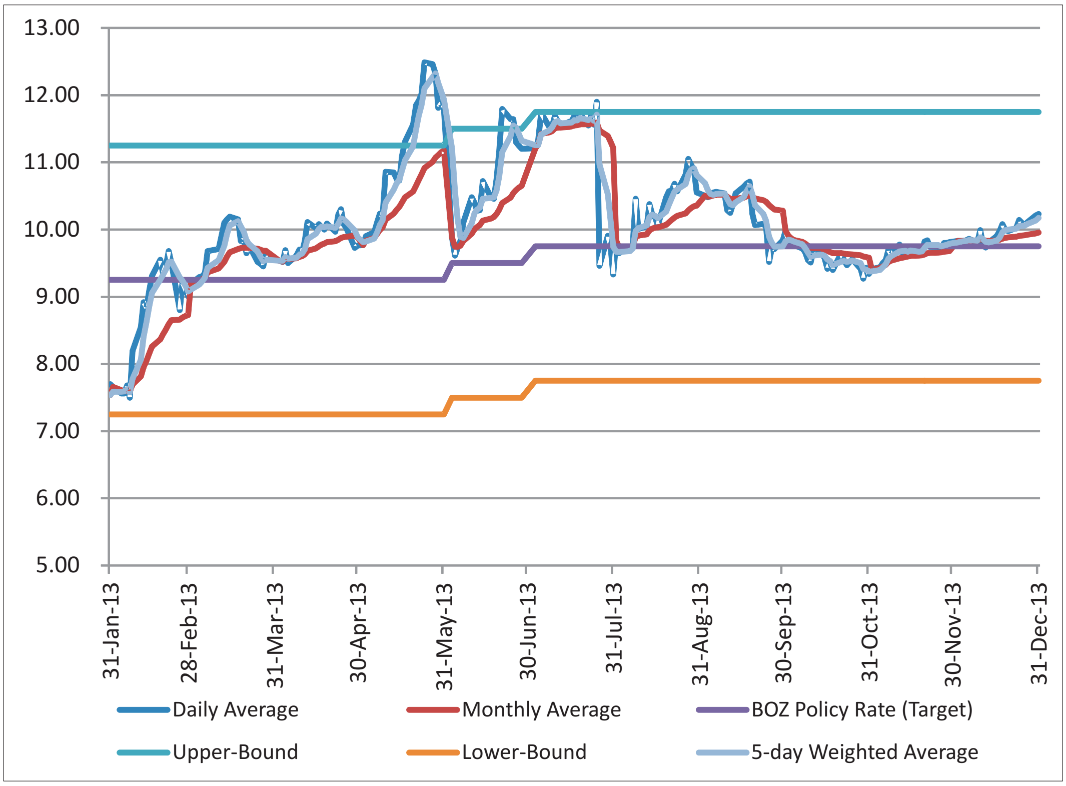
8.2 Interbank Rate, Monetary and Credit Developments

8.2.1 Overnight Interbank Rate

Monetary policy operations during the period under review were aimed at maintaining the 5-day weighted average interbank rate within a corridor of +/- 200 basis points of the Bank of Zambia (BoZ) policy rate target, which was raised to 9.75% from 9.50% in June due to rising inflationary pressures.

In order to steer the interbank rate towards the BoZ Policy Rate, the Bank offered repos and term deposits through Open Market Operations (OMO). The total OMO withdrawals amounted to K13,431.7 million for the second half of 2013, an increase from K1,320.9 million in the preceding review period as the Bank undertook more aggressive operations to address high liquidity levels in the banking system. The 5-day moving average interbank rate remained within the corridor and closed at 10.2% compared with 11.3% at end-June 2013 (see Chart 3).

Chart 3: 5-Day Average Interbank Rate and Policy Rate, Jan– Dec 2013

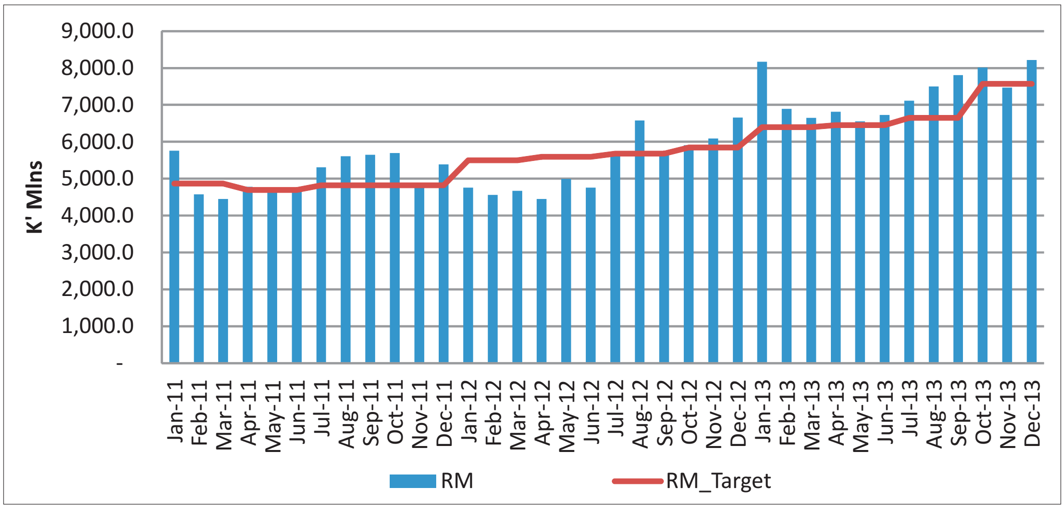


Source: Bank of Zambia

8.2.2 Reserve Money

Over the last six months of 2013, reserve money increased by 17.7% to K8,164.5 million from K6,936.5 million in the preceding half of 2013. This outturn was mainly influenced by net government spending amounting to K2,464.3 million and net purchases of foreign exchange by Bank of Zambia worth K781.1 million. These influences were however partially offset by net sales of Government securities totalling K1,329.7 million and net OMO withdrawals amounting to K858.7 million (see Chart 4).

Chart 4: Reserve Money, Jan 2011 – Dec 2013



Source: Bank of Zambia

8.2.3 Broad Money

Broad money (M3) comprehensively defined to include foreign currency deposits, rose by 11.6% to K31,042.2 million as at end-December 2013 from K27,807.8 million at end-June 2013. This outturn was largely due to an 18.3% increase in net foreign assets (NFA) which contributed 6.4 percentage points to M3 growth. The rise in NFA was attributed to an increase in commercial banks foreign assets of 6.0%. Similarly, net domestic assets (NDA) rose by 8.0%, contributing 5.2 percentage points to M3 growth. Excluding foreign currency deposits that rose by 17.2%, money supply rose by 9.6% in the period under review compared with 9.7% growth recorded in the first half of 2013 (see Table 4).

Table 4: Broad Money Developments (in K' million unless otherwise stated), Jun 2011 – Dec 2013

Description	Jun 2011	Dec 2011	Jun 2012	Dec 2012	Jun 2013	Dec 2013
Broad Money (M3)	20,340.3	21,804.8	23,004.6	25,699.0	27,807.8	31,042.2
Foreign Exchange Deposits	8,680.9	7,695.2	7,822.5	7,036.1	7,329.2	8,590.6
M3 (excl. Foreign Exchange Deposits)	11,659.3	14,109.6	15,182.1	18,662.9	20,478.6	22,451.6
6-Month Change in M3 (%)	13.5	7.2	5.5	11.7	8.2	11.6
6-Month Change in Foreign Exchange Deposits (%)	30.8	-11.4	1.7	-10.1	4.2	17.2
6-Month Change in M3 (excl. Foreign Exchange Deposits) [%]	3.4	21.0	7.6	22.9	9.7	9.6
Annual Change in M3 (%)	26.6	21.7	13.1	17.9	20.9	20.8
Annual Change in Foreign Exchange Deposits (%)	82.0	15.9	-9.9	-8.6	-6.3	22.1
Annual Change in M3 (excl. Foreign Exchange	3.2	25.1	30.2	32.3	34.9	20.3

Source: Bank of Zambia

8.2.4 Domestic Credit

Domestic credit, comprehensively defined to include foreign currency loans, rose by 8.6% during the second half of 2013 compared with an increase of 32.6% recorded in the first half of 2013. In absolute terms, domestic credit rose to K28,404.0 million in December 2013 from K26,164.7 million at end-June 2013. This was on account of the increase in lending to central government by 30.1% contributing 9.4 percentage points to domestic credit growth. However, lending to private enterprises fell by 1.1% and contributed negative 0.8 percentage points to the domestic credit outturn. Excluding foreign currency denominated loans that fell by 1.1%, domestic credit rose by 10.8% compared with 42.0% growth recorded in June 2013 (see Table 5).

Table 5: Domestic Credit Developments (in K' billion unless otherwise stated), Jun 2011 – Dec 2013

Description	Jun 11	Dec 11	Jun 12	Dec 12	Jun 13	Dec 13
Domestic Credit (DC)	14,538.7	16,822.6	18,396.3	19,726.8	26,164.7	28,404.0
O/w Foreign Exchange Credit	4,051.8	4,538.4	5,090.0	4,808.2	4,984.6	4,931.7
DC (Excl. FX Credit)	10,486.9	12,284.2	13,306.3	14,918.6	21,180.1	23,472.3
6-Month Change in Domestic Credit	-1.0	15.7	9.4	7.2	32.6	8.6
6-Month Change in Foreign Exchange Credit	-10.7	12.0	12.2	-5.5	3.7	-1.1
6-Month Change in DC (Excl. Foreign Exchange Credit)	3.4	17.1	8.3	12.1	42.0	10.8
Annual Change in Domestic Credit	6.6	14.6	26.5	17.3	42.2	44.0
Annual Change in Foreign Exchange Credit	27.3	44.8	25.6	5.9	-2.1	2.6
Annual Change in DC (Excl. Foreign Exchange Credit)	0.3	21.0	26.9	21.4	59.2	57.3

Source: Bank of Zambia

In terms of credit by sector, households (personal loans category) continued to hold the largest share of outstanding commercial bank credit, accounting for 34.5% in December 2013 compared with 32.9% in June 2013. The agricultural sector was second at 19.7% (20.5%), followed by Manufacturing 9.2% (11.1%), Wholesale and Retail Trade 9.0% (7.8%), Mining and Quarrying 6.4% (5.8%), and Transport, Storage and Communications 4.4% (4.5%) (see Appendix III, Table 4).

8.3 Foreign Exchange Market

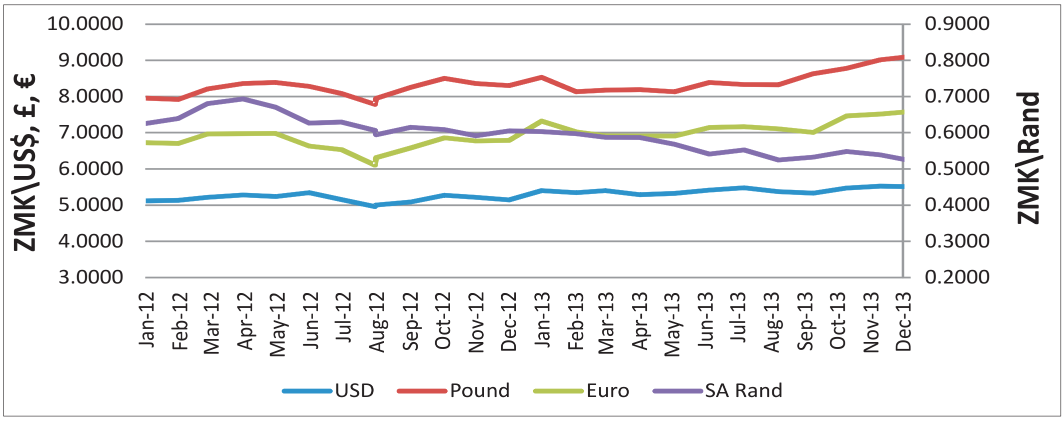
During the second half of 2013, the Kwacha was characterised by a depreciating trend against most major trade partner currencies except the rand. The weakness of the Kwacha during the review period was attributed to both local and foreign influences.

Domestically, the increase in demand for foreign exchange was influenced by high levels of liquidity in the money markets. Market participants also built long dollar positions ahead of the coming into effect of Statutory Instrument No 55 in July. Towards the end of the year, the

Kwacha remained weak largely due to continued high demand for foreign exchange fuelled by high levels of kwacha liquidity emanating mainly from a net injection of funds into the market by the central Government's implementation of the pay rise for public sector workers in September. The downgrading of Zambia's credit rating to B from B+ by Fitch Credit Rating Agencies also resulted in negative sentiment towards the local currency. On the international scene, Kwacha depreciation was influenced by a decline in the price of copper and the strengthening of the dollar globally.

Against this background, the Kwacha depreciated by 1.8% against the US dollar to close the year at K5.5126/US$ compared to K5.4172/US$ at end-June. The Kwacha also depreciated against the Pound Sterling and Euro by 8.7% and 6.3% to K9.1151/£ and K7.5920/€ from K8.3863/£ and K7.1444/€, respectively. The Kwacha however appreciated against the rand by 3.6% to close at K0.5220/ZAR (see Chart 5).

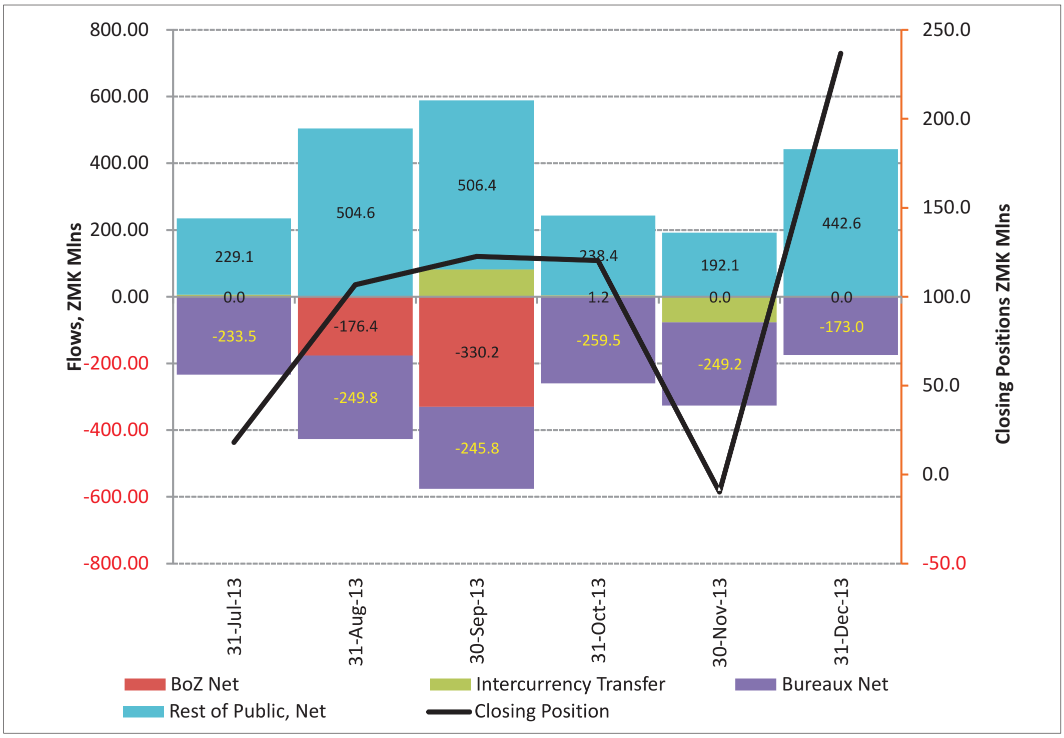
Chart 5: Exchange rates (Kwacha per foreign currency), Jan 2012 – December 2013



Source: Bank of Zambia

During the review period, banks recorded net purchases of US$1,024.9 million from the non-bank public compared with US$681.2 million in the first half of 2013. Sales to the bureaux-de-change sector increased to US$277.9 million from US$173.3 million in the first half of 2013. However, banks sold a lower amount of US$610.1 million in inter-currency transactions compared with US$638.9 million in the first half of 2013 (see Chart 6). These sales were largely accounted for in the high levels of demand for the South African rand amounting to ZAR5,522.7 million compared to ZAR4,752.4 million, previously.

Chart 6: Commercial Banks' Sources of Foreign Exchange (US$ Million)



Source: Bank of Zambia

Volatility in the domestic exchange rate marginally increased compared to the first half 2013, with the six-month moving standard deviation at K0.39 compared to K0.34. To minimise volatility in the exchange rate the BoZ intervened in the market by selling US$119.0 million. Further, due to high kwacha liquidity levels the foreign exchange market closed the year with a US$8.6 million long position from a short position of US$8.6 million at end- June 2013.

Preliminary data shows that the real effective exchange rate (REER) index depreciated by 0.9% to 96.6 in December 2013 from 95.7 recorded in June 2013 (see Table 6). This outturn was largely on account of a 2.8% depreciation in the nominal effective exchange rate index (of which the Swiss franc accounted for 2.1 percentage points), which was however, moderated by a 1.9% decline in relative prices (foreign prices relative to domestic prices).

Table 6: Annual Average Real Effective Exchange Rate, Jan 2012 - Dec 2013

	Jun-12	Dec-12	Jan-13	Jun-13	Dec-13	% Change (Jun. 13/Dec. 13)
Domestic CPI(2005=100)	181.1	186.9	188.3	194.3	200.1	3.0
Weighted Foreign CPI(2005=100)	123.1	124.2	124.0	126.1	127.5	1.1
NEER Index	2.0	2.0	2.0	1.9	2.0	3.1
REER Index (2005=100)	103.2	100.8	100.7	95.7	96.6	0.9

Source: Bank of Zambia

8.4 International Trade Developments

Preliminary data for the second half of 2013, indicate that Zambia's external sector performance was unfavourable, with the overall merchandise trade balance(c.i.f) recording a deficit of US $53.6 million compared with a surplus of US $385.6 million registered during the first half of the year (see Appendix III, Table 1). This was largely on account of a rise in the merchandise import bills as merchandise export earnings declined.

The merchandise import bills grew by 6.2% to US $5,285.5 million from US $4,975.4 million recorded during the first six months of 2013. This was due to an increase in import bills of commodity groups such as petroleum products by 57.7%, fertilisers (48.5%), iron and steel (34.2%), chemicals (33.0%), plastic and rubber products (2.7%), electrical machinery and equipment (2.1%), and industrial boilers and equipment (1.6%) (see Appendix III, Table 3).

Over the same period, merchandise export earnings, at US $5,231.9 million, were 2.4% lower than US $5,361.1 million recorded during the first half of 2013, due to a decline in non-traditional export earnings.

Non-traditional export earnings, at US $1,692.2 million, were 6.7% lower than US $1,814.2 million registered during the first half of 2013, largely on account of a decline in earnings from the export of copper wire, fresh flowers, fresh fruits and vegetables, cane sugar, electric cables, gemstones, maize, and cement.

Similarly, copper export earnings marginally declined to US $3,464.8 million from US $3,476.5 million during the first half of the year, largely due to lower realised prices. The realised average prices of copper, declined by 5.3% to US $6,888.46 per ton (US $3.12 per pound) from US $7,268.71 per ton (US $3.30 per pound) during the first half of the year. Copper export volumes, however, grew by 5.2% to 502,982.62 metric tons (mt) from 478,357.98 mt recorded during the first half (see Appendix III, Table 2).

However, cobalt export earnings rose by 6.4% to US $74.9 million from US $70.4 million, driven by higher realised prices. The average realised price of cobalt increased by 10.5% to US $24,841.97 per ton (US $11.27 per pound) from US $22,475.83 per ton (US $10.19 per pound) recorded during the first half of 2013. Cobalt export volumes, however, fell by 3.7% to 3,015.15 mt compared with 3,131.14 mt recorded during the first six months of 2013 (see Appendix III, Table 2).

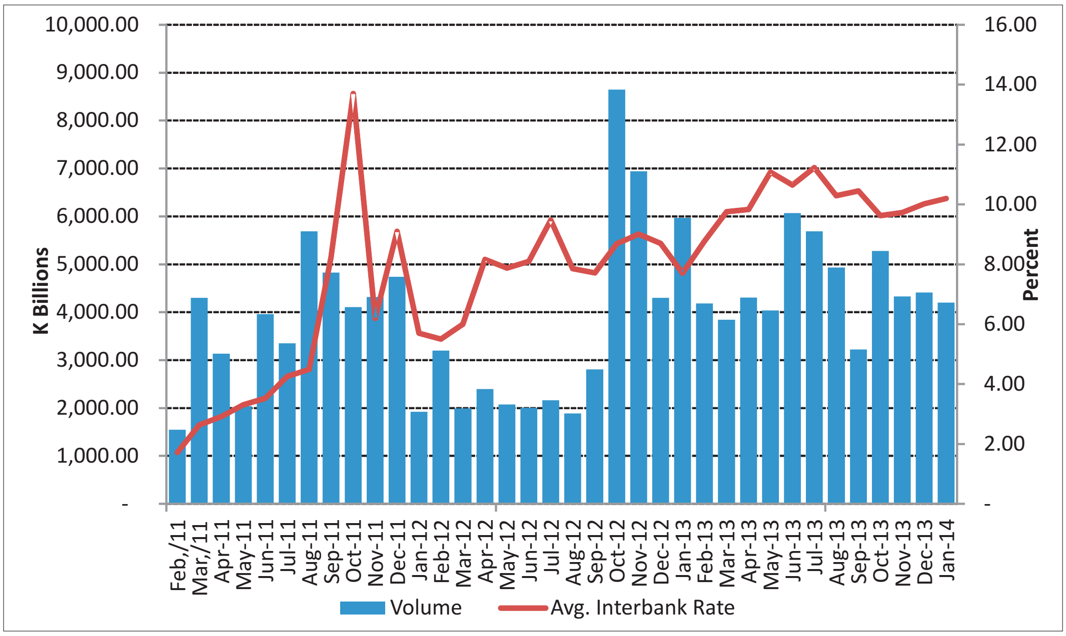
8.5 Money and Capital Markets Developments

8.5.1 Money Markets

Interbank market

The volume of funds traded by commercial banks in the interbank money market increased to K27,966.8 million in the second half of 2013 from K25,919.1 million in the first half of 2013. The funds were traded at an average rate of 10.27% from an average of 9.75% in the preceding period. During the review period, the market remained most active at shorter maturity with K25,181.5 million traded on an overnight basis. At the close of December 2013, the overnight interbank rate increased further to close at 10.21% compared to 9.71 % at end-June 2013, explained by the tight liquidity conditions attributed in part to high concentration of funds in a few banks which were not trading on the interbank due to exhausted credit lines.

Chart 7: Interbank Money Market Activity



Source: Bank of Zambia

Overnight Lending Facility

Over the last six months of 2013, the amount of funds accessed on the overnight lending facility window declined. A total of K3,092.4 million in short-term relief funds was borrowed from the Bank of Zambia, compared with K3,967.2 million borrowed in the first half of 2013. These funds were advanced at 12.50% while the BoZ Policy rate was maintained at 9.75% throughout the review period.

Government Securities Market

The total value of Treasury bills placed on offer increased to K7,200.0 million from K5,550.0 million during the first half of 2013, as the tender size at each auction was raised to K600.0 million from K450.0 million previously. In response to the tender invitations, investors submitted bids amounting to K6,545.3 million. This translated into a subscription rate of 90.9% compared with a subscription rate of 134.3% in the preceding review period. Total sales to the market were recorded at K5,714.0 million against maturities of K4,978.1 million.

With regard to Government bonds, securities worth K1,840.0 million were placed on offer, compared to the K1,300.0 million offered previously. Investors placed bids worth K1,398.0 million, reflecting a subscription rate of 76.0%, lower than the 129.7% subscription rate recorded in the first half of 2013 (see Table AIII.7). Out of the bids received, K1,031.3 million was accepted against a maturity of K746.0 million.

Stock of Government Securities

For the period under review, a surplus of K1,020.4 million was realised in net sales of Government securities in the primary market. As a result, the total stock of Government securities in circulation rose by 12.5% to K19,372.0 million from K17,226.7 million recorded at end-June 2013. The stock of Treasury bills in circulation increased by 20.5% to K9,942.9 million compared with an increase of 20% to K17,226.7 million in the first half of 2013. Similarly, the stock of Government bonds outstanding rose by 5.1% to K9,429.1 million compared with an increase of 19.4% to K8,975.6 million, previously.

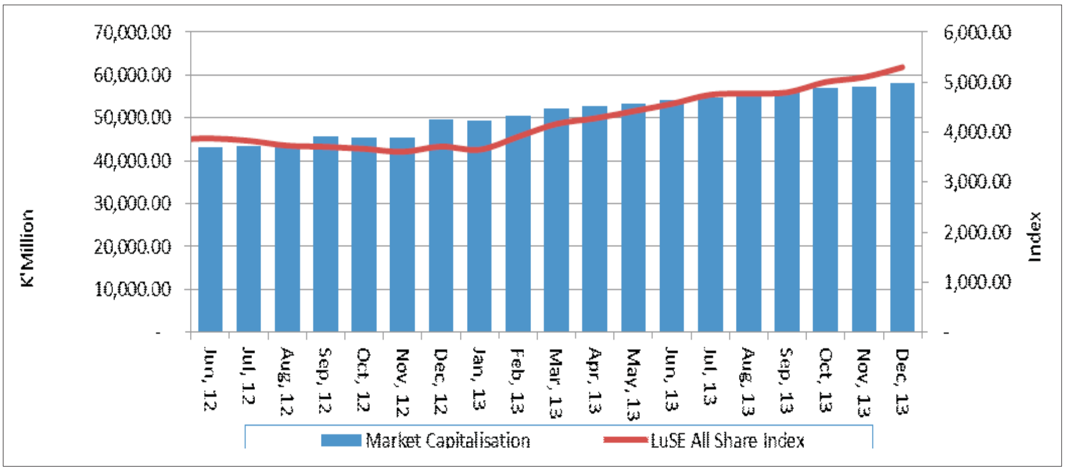
In terms of investor distribution, commercial banks accounted for the largest proportion, with a holding of K9,974.6 million representing 51.5% of the total securities outstanding. The non-bank public accounted for K7,042.1 million (36.4%) while the Bank of Zambia accounted for K2,355.3 million or 12.2% of the total outstanding securities.

8.5.2 Capital Market

The stock market extended the gains posted in the first half of the year into the last half of 2013. Market capitalisation increased by 7.4% to K58,188.0 million from the end-June position of K54,179.0 million; while the Lusaka Stock Exchange (LuSE) All Share Index went up by 16.0% to 5,300.1 from 4,568.0 (see Chart 8). The largest share price increases were registered by Real Estate Investments Zambia (REIZ) (formally Farmers House) whose share price rose by 187.2% to K13.50, British American Tobacco by 98.3% to K4.76, Lafarge by 68.4% to K15.75 and African Explosives by 51.5% to K6.85. The main losers were National Breweries and Investrust with share prices falling by 92.8% and 24.8%, respectively.

Non-resident investors withdrew a net US$1.6 million from the stock exchange compared with a net withdrawal of US$6.1 million recorded in the first half of 2013.

Chart 8: LUSE Indicators, June 2012 – Dec 2013



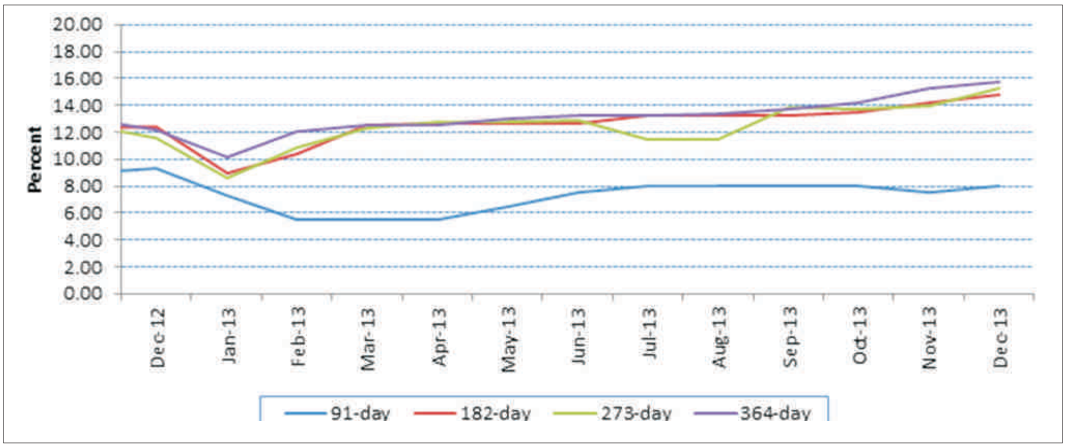
Source: Bank of Zambia

8.6 Interest Rates

8.6.1 Government Securities Interest rates

Yield rates on Treasury bills trended upwards in 2013, particularly in the latter half of the year, due to increases in tender size, which signalled huge appetite for funds. Yield rates for the 91- and 182-day bills closed the year at 8.0% and 14.8% compared with 7.5% and 12.7% at end-June 2013. The yield rates for 273- and 364-day bills increased to 15.2% and 15.8% compared to 12.9% and 13.3% at the close of the previous review period. Consequently, the weighted average Treasury bill yield rate for the review period increased to 15.3% from 13.1% previously (see Chart 9).

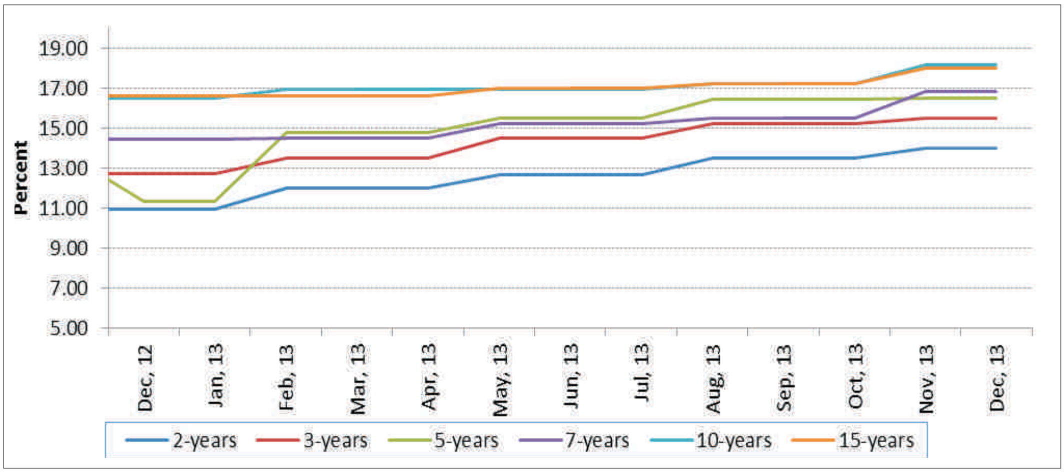
Chart 9: Treasury bill yield rates (% p.a), Dec 2012 – Dec 2013



Source: Bank of Zambia

Similarly, yield rates on Government bonds recorded an increase in the second half of 2013. The yield rates on 2-year and 3-year paper rose to 14.0% and 15.5% from 12.7% and 14.5% respectively, while yield rates for the 5, 7 and 10 year tenors increased to 16.5%, 16.9% and 18.2% from 15.5%, 15.2% and 17.0%, respectively, in the first half of the year. Yield rates on the 15-year paper also went up to 18.0% from 17.0%, in the preceding period. In view of the upward trend in individual yield rates, the weighted average bond yield rate closed higher at 16.3% from 15.2% (see Chart 10).

Chart 10: Government bond yield rates (% p.a), Dec 2012 – Dec 2013

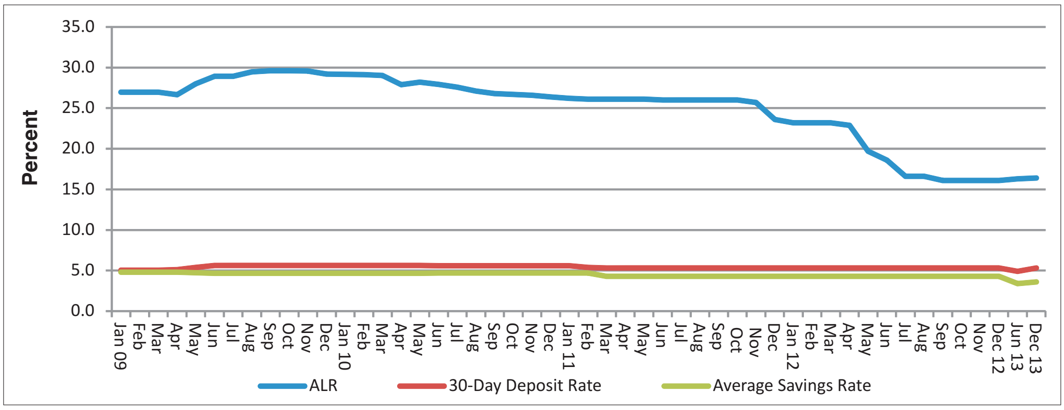


Source: Bank of Zambia

8.6.2 Commercial Banks Interest Rates

The Average Lending Rate (ALR) increased to 16.4% in December 2013 from 16.3% in June 2013. Similarly, both the Average Savings Rate (ASR) for amounts above K100.00 and the 30-day deposit rate for amounts exceeding K20 000.00 rose to 3.6% and 5.3% from 3.4% and 4.9%, respectively (see Chart 11).

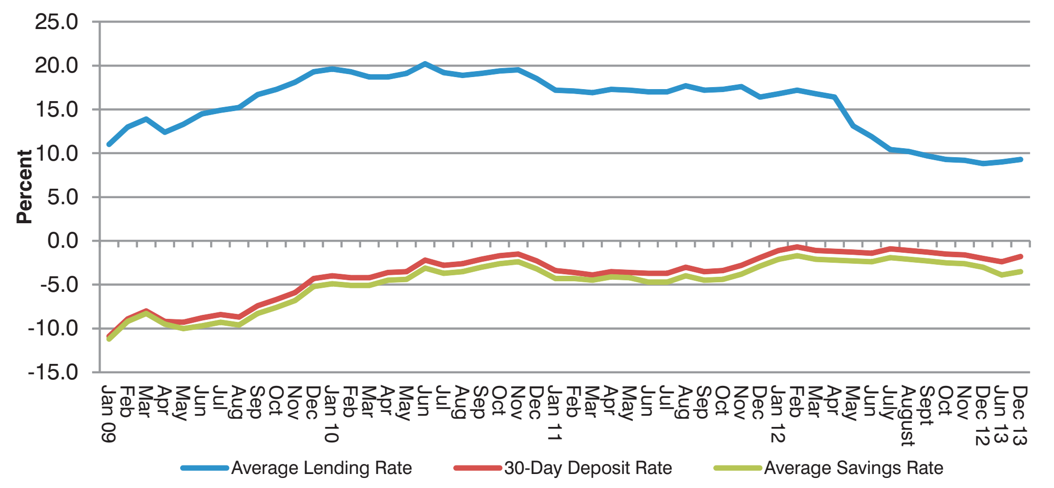
Chart 11: Lending and Saving Rates, Jan 2009- Dec 2013



Source: Bank of Zambia

In real terms, all monitored interest rates rose as inflation declined to 7.1% in December 2013 from 7.3% in June 2013. The real ALR rose to 9.3% from 9.0% in June 2013. Similarly, the real ASR for amounts above K100.00 and the real 30-day deposit rate for amounts above K20 000.00 rose to -3.5% [-3.9%] and -1.8% [-2.4%], respectively (see Chart 12).

Chart 12: Real Interest Rates (%), Jan 2009 - Dec 2013



Source: Bank of Zambia

8.6.3 Non-Bank Financial Institutions Lending Rates

In the second half of 2013, the total cost of credit in the non-bank financial institutions (NBFIs) sector (measured as the average effective annual interest rate) decreased by 1.8 percentage points to 24.7% per annum from 26.5% per annum in the first half of 2013 (see Table 7). The decrease in the cost of credit was attributed to the introduction of interest rate caps, effective January 2013 and applicable to new loans. The decrease in the cost of credit resulted in a 76.9% rise in the volume of loans extended by NBFIs to K3,934.8 million in the second half of 2013 from K2,224.5 million in the first half of 2013.

Table 7: Average Annual Effective Interest Rates (%)

Description	First Half 2013	Second Half 2013
Microfinance Institutions	38.3	34.3
Leasing Finance Institutions	24.7	25.9
Building Societies	21.7	20.8
Development Bank of Zambia	20.6	15.5
National Savings and Credit Bank	27.0	27.0
Overall for the sector	**26.5**	24.7

Source: Bank of Zambia

9.0 Fiscal Developments

Preliminary data indicate that the Central Government budget recorded a deficit of K3,192.9 million during the second half of 2013 against the programmed deficit of K4,806.0 million (see Appendix III, Table 5). This performance was explained by lower than programmed expenditure.

Total revenues and grants at K14,372.2 million were 11.0% below the programmed amount of K16,154.4 million, largely explained by the delayed disbursement of external grants, particularly project support. Total grants were K190.9 million, thus 91.4% below the programmed level of K2,226.2 million. Similarly, tax revenues at K12,956.3 million were 1.6% below target, mainly reflecting lower than programmed income (corporate) tax, customs and excise duty.

Non-tax revenues, however, at K1,225.0 million were 60.1% above the target of K765.4 million, mainly due to favourable collections under user fees and charges.

Total expenditures during the review period were K17,358.7 million, 26.5% lower than the programmed amount of K23,629.7 million. This was mainly due to lower expenditure on capital projects, notably rural electrification programme, railway line rehabilitation, water and sanitation. Spending on non-financial assets at K3,172.5 million was 58.2% lower than programmed amount of K7,595.5 million.

Consistent with restrained expenditures in the period under review, total financing at K3,192.9 million, was 33.6% lower than the programmed financing of K4,806.0 million. The total financing comprised domestic financing of K3,554.6 million and net foreign debt amortisation of K361.7 million.

Appendix I: Selected Macroeconomic Indicators

Description/Years	Dec-11	Dec-12	Jan-13	Feb-13	Mar-13	Apr-13	May-13	Jun-13	Jul-13	Aug-13	Sep-13	Oct-13	Nov-13	Dec-13
Monetary Aggregates (K'bn)														
Reserve money (end-period in K'billion)*	5 385.4	6 740.7	8 246.5	6 488.0	7 012.6	6 878.9	6 450.2	6 281.2	7 110.9	7 500.0	7 809.3	8 012.7	7 465.1	8 218.7
Growth Rate	11.6	#REF!	22.3	-21.3	8.1	-1.9	-6.2	-0.7	2.6	5.5	-1.9	2.4	-6.8	10.1
Broad money (in K'billion)	21 804.78	25 699.0	25 237.0	27 565.0	25 809.6	25 809.6	26 507.1	27 795.7	28 662.5	29 248.4	28 950.6	29 577.0	29 466.9	31 042.2
Growth Rate	1.4	#REF!	-1.8	9.2	-6.4	2.7	0.6	4.3	3.1	2.0	-1.0	2.2	-0.4	5.3
Net Claims on Government (in K'billion)	5 200.10	3 242.15	4 952.92	6 121.67	5 474.32	6 571.00	7 432.60	7 929.70	7 957.70	7 848.50	8 151.60	8 741.50	8 979.80	10 335.16
Prices (%)														
Inflation	7.2	7.3	7.0	6.9	6.6	6.5	7	7.3	7.3	7.1	7	6.9	7.0	7.1
Nominal Interest and yield rates (aver. %)														
Commercial Banks ' rates														
Commercial banks' weighted lending base rate	16.6	8.8	9.3	9.3	9.3	9.3	9.3	9.5	9.8	9.8	9.8	9.8	9.8	9.8
Average Savings rate (>K100,000)	4.3	4.3	4.3	4.3	3.3	2.6	3.0	3.4	3.3	3.2	3.3	2.7	3.0	2.9
Deposit rate (30 days, over K20 million)	5.3	5.3	5.3	5.3	4.5	4.6	4.7	4.9	4.7	5.0	4.7	5.0	5.0	5.3
Treasury bill yield rates														
Weighted TB rate	11.7	11.8	9.3	10.9	12.0	12.5	12.5	12.7	12.8	13.2	13.2	13.6	14.3	15.2
91-day	7.1	9.5	7.3	5.5	5.5	5.5	6.5	7.5	8.0	8.0	8.0	8.0	7.6	8.0
182-day	9.8	12.2	9.0	10.4	12.5	12.6	12.6	12.7	13.3	13.2	13.3	13.4	14.1	14.8
273-day	11.4	11.2	8.6	10.9	12.3	12.8	12.8	12.9	11.5	11.5	13.9	13.8	14.1	15.0
364-day	13.4	11.7	10.2	12.1	12.5	12.5	12.9	12.9	13.3	13.3	13.8	13.9	15.2	15.7
Government bonds Yield Rates														
Weighted Bond Yield Rate	15.0						5.7							
2 year	14.7	11.0	11.0	11.2	12.0	12.0	12.7	12.7	12.7	13.5	13.5	13.5	13.7	14.0
3 year	15.1	12.6	12.8	12.9	13.5	13.5	14.5	14.5	14.5	15.3	15.3	15.3	15.4	15.5
5 year	15.4	13.5	13.5	13.8	14.8	14.8	15.5	15.5	15.5	16.5	16.5	16.5	16.5	16.5
7 year	15.0	14.5	14.5	14.5	14.5	14.5	15.5	15.2	15.2	15.5	15.5	15.5	16.0	16.9
10 year	15.9	16.5	16.5	16.6	17.0	17.0	17.0	17.0	17.0	17.3	17.3	17.3	17.6	18.2
15 year	16.2	16.6	16.6	16.6	16.6	16.6	17.0	17.0	17.0	17.3	17.3	17.3	17.6	18.0
Real Interest and Yield Rates (%)														
Commercial Banks' rates														
Commercial banks' weighted lending base rate	9.4	1.5	2.3	2.4	2.7	2.8	2.8	3.0	3.3	3.3	3.3	3.3	3.3	3.3
Average savings rate	-2.9	-3.0	-2.7	-2.6	-3.3	-3.9	-3.5	-3.1	-3.2	-3.3	-3.2	-3.8	-3.5	-3.6
Deposit rate (30 days, over K20 million)	-1.9	-2.0	-1.7	-1.6	-2.1	-1.9	-1.8	-1.6	-1.8	-1.5	-1.8	-1.5	-1.5	-1.2
Treasury bill yield rates														
Weighted TB rate	4.5	4.5	2.3	4.0	5.4	6.0	6.0	6.2	6.3	6.7	6.7	7.1	7.8	8.7
91-day	-0.1	2.2	0.7	-1.4	-1.1	-1.0	0.0	1.0	1.5	1.5	1.5	1.5	1.1	1.5
182-day	2.6	4.9	4.0	3.5	5.9	6.1	6.1	6.2	6.8	6.7	6.8	6.9	7.6	8.3
273-day	4.2	3.9	2.8	4.0	5.7	6.3	6.3	6.4	5.0	5.0	7.4	7.3	7.6	8.5
364-day	6.2	4.4	3.2	5.2	5.9	6.0	6.4	6.4	6.8	6.8	7.3	7.4	8.7	9.2
Government bonds Yield Rates														
Weighted Bond rate	7.8													
2 year	7.5	3.7	4.0	4.3	5.4	5.5	6.2	6.2	6.2	7.0	7.0	7.0	7.2	7.5
3 year	7.9	5.3	5.8	6.0	6.9	7.0	8.0	8.0	8.0	8.8	8.8	8.8	8.9	9.0
5 year	8.2	6.3	6.5	6.9	8.2	8.3	9.0	9.0	9.0	10.0	10.0	10.0	10.0	10.0
7 year	7.8	7.2	7.5	7.6	7.9	8.0	9.0	8.7	8.7	9.0	9.0	9.0	9.5	10.4
10 year	8.7	9.2	9.5	9.7	10.4	10.5	10.5	10.5	10.5	10.8	10.8	10.8	11.1	11.7
15 year	9.0	9.3	9.6	9.7	10.0	10.1	10.5	10.5	10.5	10.8	10.8	10.8	11.1	11.5
Exchange rates (average K/US $)														
Commercial banks' interbank mid-rate	5118.5	5 208.5	5.31											
Bank of Zambia mid rate**	5117.3	5 146.6	5.40	5.35	5.40	5.29	5.32	5.42	5.48	5.43	5.33	5.32	5.52	5.54
Real sector														
Mining output (tonnes)														
Copper	64 866.4	69 617.2	74 929.8	66 362.3	74 417.7	73 002.0	87 811.8	81 377.2	81 036.4	78 736.8	85 515.0	98 660.9	87 927.7	90 701.2
Cobalt	534.6	385.3	576.2	576.2	540.5	587.7	482.0	528.2	586.7	492.3	440.2	692.2	447.0	526.5
Metal Earnings (US $'000)														
Copper	463.4	536, 700.00	593 513.2	569 501.1	609 813.4	673 327.6	541 955.2	488 936.1	510 862.5	543 637.8	574 477.6	687 345.9	559 493.0	588 961.1
Cobalt	15.0	31, 300.00	12 207.8	11 984.0	11 791.7	11 837.1	11 666.4	10 881.9	9 976.1	11 177.4	11 798.7	16 759.5	11 440.2	13 750.4
Total	478.4	568, 000.00	602 400.0	512 500.0	601 000.0	599 000.0	553 621.6	499 818.0	520 838.5	554 815.1	586 276.3	704 105.4	570 933.2	602 711.5
External sector (US $ mn)														
Trade Balance	15.5	281.0	80.5	92.2	51.0	69.1	63.7	29.2	30.1	4.4	0.7	3.9	-72.0	-20.7
Exports, c.i.f	614.0	1 024.9	868.5	899.1	889.0	933.8	931.2	839.5	853.4	836.0	916.0	968.0	798.6	859.9
Imports, c.i.f	-598.5	743.9	-788.0	-806.9	-838.1	-864.7	-867.5	-810.2	-823.3	-831.6	-915.3	-964.1	-870.6	-880.5
Source: Bank of Zambia Statistics Fortnightly														
* Reserve money is narrowly defined.														
**Based on BoZ end of period mid-exchange rate														

Appendix II: Zambia's Economic Programme

A mission from the International Monetary Fund (IMF) visited Zambia from 17th to 24th September 2013 to conclude the 2013 Article IV consultations that started in July 2013. The IMF mission and Zambian authorities discussed issues related to monetary policy, international reserves, competitiveness, growth and inflation projections. They also discussed issues regarding Statutory Instrument 55, government's plans for addressing fiscal challenges, deficit financing impact on monetary policy and the lending rate ceiling introduced by the BoZ.

An IMF staff report for the 2013 Article IV Consultations and a Debt Sustainability Analysis report have since been released for public information on the website. The Staff Report concludes that the Zambian economy is still performing well with strong growth although there are major risks to the outlook including uncertainties about fiscal policy and the possible slowdown in emerging markets which may have an effect on copper prices. The Fund recommends in its report undertaking of fiscal policy reforms to contain the anticipated expenditures, boost revenue and create fiscal space for infrastructure development as well as monetary forms that allow more exchange rate flexibility, reserve build up and tightening of monetary policy by the central bank to contain inflation. The Fund also raised issues of the country's competitiveness which have been hampered by some regulations, high minimum wages and policy direction.

The Debt Sustainability Analysis (DSA) report indicates that Zambia's external debt is still sustainable, as the risk of its debt distress remains low. The report reveals that all debt indicators remain below the indicative policy threshold throughout the projection period 2013-2033. However, the Fund recommends that Zambia needs to maintain sound macroeconomic policies, strong debt management, a higher diversification of export base and project appraisal capacity in order to maintain debt sustainability in light of expected increase in non-concessional borrowing and potential external shocks.

Zambia received US $8.2 million Poverty Reduction Budget Support (PRBS) from Germany in the second half of 2013. In addition, a total of US $60.0 million mining tax revenue was received from Kansanshi Mining Plc, compared to US $71.4 million received in the first half of 2013. Other foreign exchange inflows came from Bank of Zambia foreign exchange purchases from the market amounting to US $138.0 million and US $144.4 million purchased from the Government (funds borrowed by Government from ZESCO).

The above receipts were against major foreign exchange outflows including payments to PTA Bank for oil procurement arrears (US $70.0 million), Bank of Zambia sales to the market (US $20.0 million) and debt service payments to various creditors (US $149.7million).

With regards to performance of the economic programme, preliminary data indicate that the Net Domestic Assets (NDA) of the Bank of Zambia, the Net Domestic Financing (NDF) of Government and the Unencumbered International Reserves (UIR) quantitative performance criteria were off track as at end-December 2013. The average NDA was K280.6 million above the end-December 2013 programme ceiling of K1,155.0 million whilst the NDF stood at K15,912.1 million and was K5,075.6 million above the end-December 2013 adjusted ceiling of K10,836.5 million. The UIR at US $2,385.6 million, were US $137.9 million below the end-December 2013 adjusted floor of US $2,523.5 million. The NDA and NDF were affected by net government spending and declining Net Foreign Assets whilst the performance in the UIR was largely explained by Bank of Zambia foreign exchange sales to the market and debt service payments to various creditors despite having foreign exchange receipts from the mines, BOZ foreign exchange purchases and other receipts.

Table AII.1: Macroeconomic Outturn and Targets in 2013, and Targets for 2014

	End –December 2013 Targets	End-December 2013` Outturn	End-December 2014
Description	7.0	6.8	Targets
Real GDP growth rate (%)	6.0	7.1	7.0
CPI Inflation, end period (%)		7.0	6.5
CPI Inflation, annual average (%)	4.0	3.1	7.0
Gross Official Reserves (in months of imports)	18.2	20.8	3.0
Broad Money growth (%)	4.3		19.6
Budget deficit, excluding grants (% of GDP)	1.5		7.8

Source: Bank of Zambia, Budget Speech, 2014, IMF Staff Report Article IV Consultations 2013

Appendix III: Statistical Tables and Charts

Table AIII.1: Trade Data in US $ million (c.i.f), Jan 2012 – Dec 2013

	Jan-Jun 2012	July -Dec 2012	Jan-June 2013	July-Dec 2013*	Change
Trade Balance	210.7	332.4	385.6	-53.6	-113.9
Exports, c.i.f	4,327.7	5,021.6	5,361.1	5,231.9	-2.4
Metals	3,065.1	3,432.5	3,546.9	3,539.7	-0.2
Copper	2,981.0	3,313.5	3,476.5	3,464.8	-0.3
Cobalt	84.1	119.0	70.4	74.9	6.4
Total NTEs	1,262.6	1,589.1	1,814.2	1,692.2	-6.7
Exporter Audit Adjustor	-13.2	-13.2	-13.2	-13.2	0.0
Total	1,275.8	1,602.3	1,827.4	1,705.4	-6.7
Copper Wire	67.8	83.7	68.3	55.1	-19.3
Cane Sugar	49.8	92.0	85.6	103.4	20.8
Burley Tobacco	76.7	79.9	79.7	133.6	67.7
Cotton Lint	22.9	106.2	34.0	57.7	69.8
Electrical Cables	16.9	34.0	28.7	24.4	-15.0
Fresh Flowers	12.3	11.4	26.7	5.8	-78.1
Cotton Yarn	0.0	0.0	0.0	0.0	-100.0
Fresh Fruits & Vegetables	4.3	11.4	26.7	4.8	-82.0
Gemstones	94.9	137.4	141.3	74.5	-47.3
Gasoil/Petroleum Oils	65.3	31.8	50.4	55.5	10.2
Electricity	24.0	18.7	41.4	36.6	-11.5
Other	840.9	995.7	1,244.7	1,153.9	-7.3
Of which Maize & Maize Seed	335.9	0.0			
Wheat & Meslin	15.6	106.6	104.6	41.5	-60.3
Cement & Lime	21.8	19.7	9.2	8.4	-8.3
Gold	23.1	4.8	126.2	112.7	-10.7
Imports c.i.f.	-4,117.0	-4,689.2	-4,975.4	-5,285.5	6.2

Source: Bank of Zambia
*Figures are preliminary

Table AIII.2: Metal Production, Export Volumes, Values and Prices; Jan 2012 – Dec 2013

Period	Copper				Cobalt			
	Exports Volumes Tonnes	Exports US $'000	Price US$/Tonne	Price US$/pound	Exports Volumes Tonnes	Exports US $ '000	Price US$/Tonne	Price US$/ pound
Quarter 1, 2012	200,834.20	1,510,969.50	7,523.47	3.41	2,034.70	43,775.00	21,514.29	9.76
Quarter 2, 2012	206,179.00	1,470,037.45	7,129.91	3.2	1,613.60	40,334.77	24,997.52	11.34
Jan - Jun 2012	407,013.20	2,981,007.00	7,324.10	3.32	3,442.00	84,109.80	24,436.22	11.08
Quarter 3, 2012	249,524.20	1,779,118.20	7,130.04	3.23	2,624.20	62,263.20	23,726.23	10.76
Quarter 4, 2012	225,557.70	1,534,367.70	6,802.55	3.09	2,284.10	56,757.50	24,848.44	11.27
Jul - Dec 2012	475,081.90	3,313,485.80	6,974.56	3.16	4,908.40	119,020.70	24,248.46	11.0
Quarter 1, 2013	233,848.30	1,772,827.70	7,581.10	3.44	1,699.30	35,983.40	21,175.43	9.61
Quarter 2, 2013	244,509.70	1,704,218.80	6,969.94	3.16	1,431.80	34,385.30	24,014.76	10.89
Jan - Jun 2013	478,358.00	3,477,046.60	7,268.71	3.3	3,131.10	70,368.80	22,473.83	10.19
Quarter 1, 2013	236,459.50	1,628,977.80	6,889.00	3.1	1,349.40	32,952.20	24,419.40	11.08
Quarter 2, 2013*	266,523.10	1,835,800.00	6,888.00	3.1	1,665.70	41,950.10	25,184.30	11.42
Jul - Dec 2013*	502,982.60	3,464,777.80	6,888.50	3.1	3,015.10	74,902.20	24,842.00	11.27

Source: Bank of Zambia Statistics Fortnightly
*Figures are preliminary

Table AIII.3: Imports by Commodity Groups in US $ millions (c.i.f.); Jan 2012 – Dec 2013

Description	Jan-Jun 2012	July Dec 2012	Jan-Jun 2013	July-Dec 2013	%Change
Food Items	231.7	273.1	229.0	229.1	0.0
Petroleum Products	373.4	561.9	465.9	734.6	57.7
Fertilizers	136.7	167.5	157.6	234.1	48.5
Chemicals	456.1	450.1	429.9	571.8	33.0
Plastic and Rubber Products	213.8	220.7	246.8	253.5	2.7
Paper and Paper Products	70.0	67.1	77.4	66.1	-14.6
Iron and Steel	280.2	289.0	333.5	447.6	34.2
Industrial Boilers & Equipment	733.2	774.7	908.3	922.7	1.6
Electrical Machinery & Equipment	238.9	258.7	307.0	313.4	2.1
Vehicles	369.5	505.8	497.3	391.0	-21.4
Other Imports	1,013.4	1,120.4	1,322.8	1,121.7	-15.2
Total Imports	**4,117.0**	**4,689.2**	**4,975.4**	**5,285.5**	**6.2**

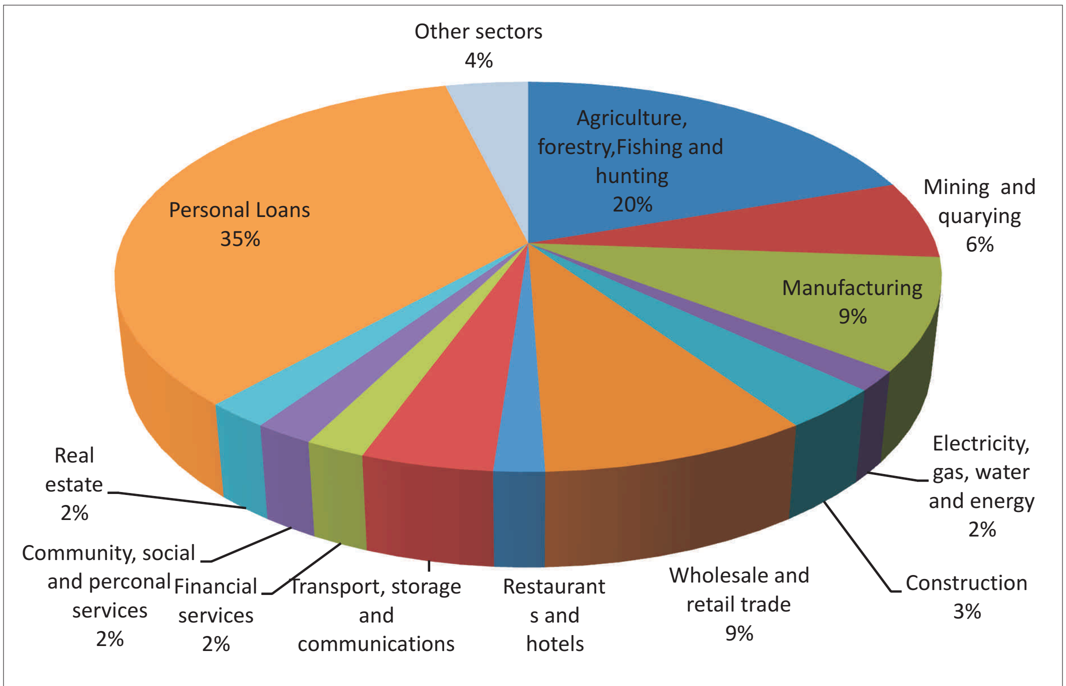
Source: Bank of Zambia
*Figures are preliminary

Table AIII.4: Shares of Total Loans and Advances by Sector (Excluding Foreign Currency Loans), Jun 2011 – Dec 2013 (%)

Sector	Jun-11	Dec-11	Jun-12	Dec-12	Jun-13	Dec-13
Agriculture, forestry, fishing & hunting	12.0	13.1	9.4	21.1	20.5	19.7
Mining & Quarrying	1.5	0.9	1.2	1.4	5.8	6.4
Manufacturing	10.5	6.9	7.0	6.8	11.1	9.2
Electricity, Gas, Water & Energy	1.2	1.7	2.3	1.5	1.7	1.6
Construction	5.8	3.3	3.3	3.1	3.5	3.4
Wholesale & Retail Trade	10.4	9.7	9.2	6.7	7.8	9.0
Restaurants & Hotels	1.7	1.5	1.4	0.9	1.7	1.7
Transport, Storage & Comm	5.8	4.0	4.1	4.4	4.5	4.4
Financial Services	2.0	2.9	2.9	1.9	2.0	2.0
Community, Soc & PersServices	4.2	2.4	2.5	2.3	2.3	2.0
Real Estate	5.6	1.7	1.8	1.9	2.1	2.1
Personal Loans	37.0	47.8	50.7	43.9	32.9	34.5
Others	2.4	4.1	4.2	4.0	4.2	3.8

Source: Bank of Zambia

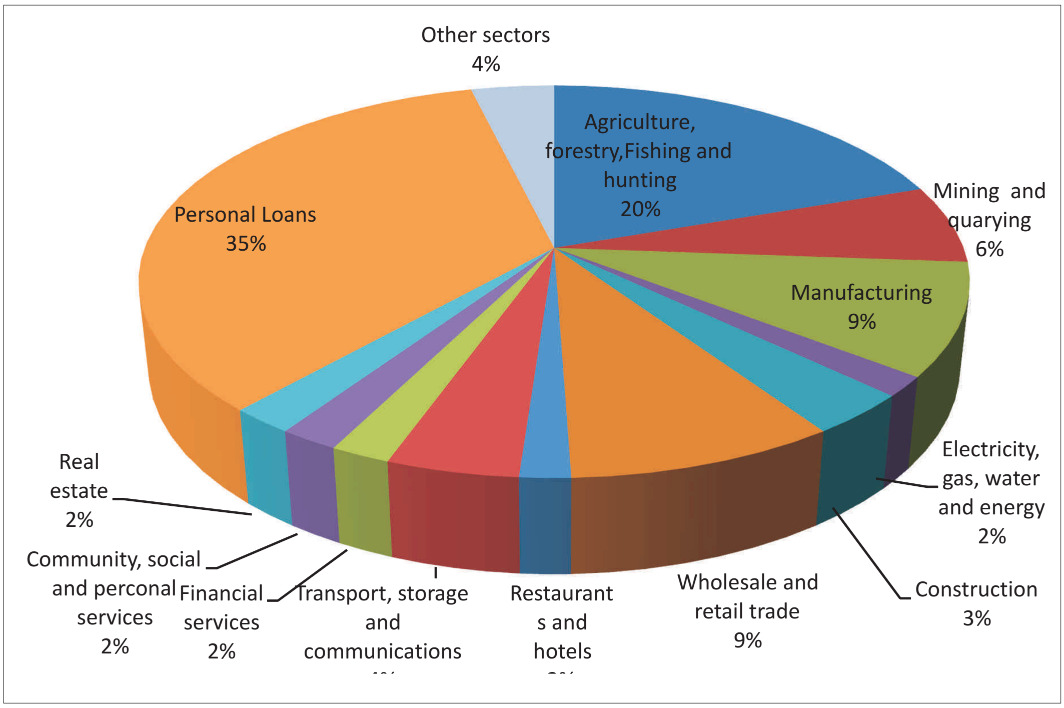
Chart AIII.1: Structure of Loans and Advances, December 2013



Source: Bank of Zambia

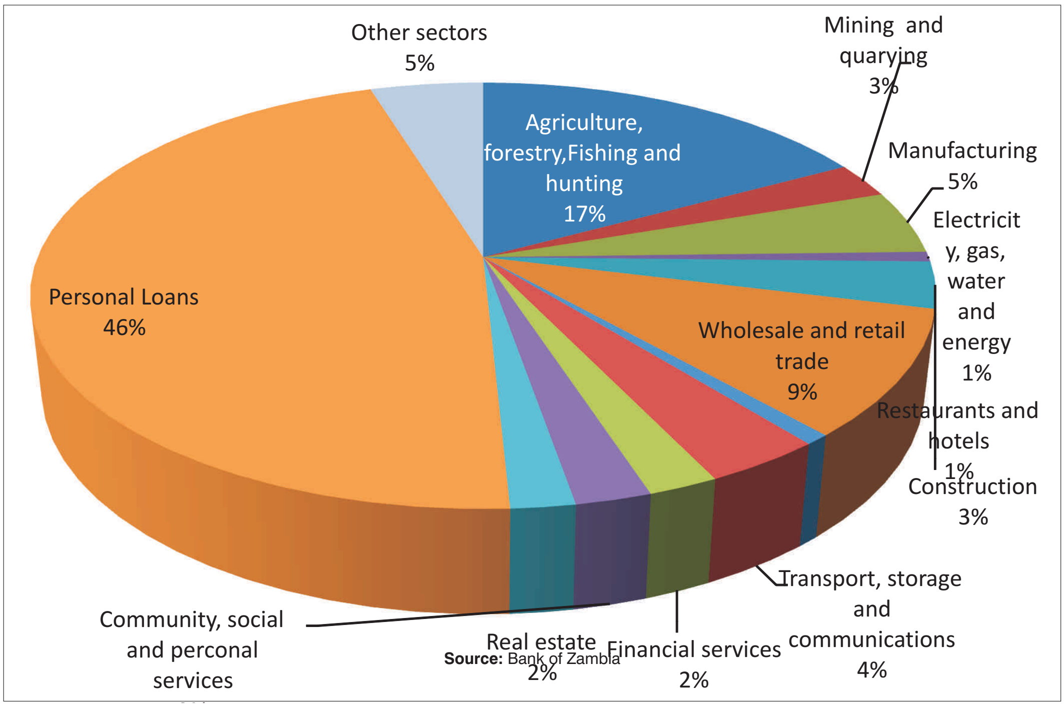
Monetary Policy Statement

Chart AIII.2: Structure of Loans and Advances, (Excluding Foreign Currency Loans) December 2013



Source: Bank of Zambia

Chart AIII.3: Structure of Forex Loans and Advances December 2013



Source: Bank of Zambia

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Table AIII.5: Central Government Fiscal Operations, Second Half 2013 (K'million)

	2013 Budget	First Half 2013		Second Half 2013		
	Projection	Proj	Prelim	Proj	Prelim	Var %
Revenue and Grants	26 271.4	12 868 617	10 983.8	16 154.4	14 372.2	-11.0
Tax Revenue	23 535.9	11 550.9	10 152.2	13 162.8	12 956.3	-1.6
Non Tax Revenue	1 210.0	701.3	570.5	765.4	1 225.0	60.1
Grants	1 525.5	697.7	261.1	2 226.2	190.9	-91.4
Total Expenditure	31 685.3	16 976.7	14 967.1	23 629.7	17 358.7	-26.5
Current Expenditure	22 131.5	11 285.0	11 457.4	15 389.4	13 809.2	-10.3
Personal Emoluments	11 015.6	5 302.8	5 031.2	6 951.7	6 865.8	-1.2
Public Service Retrenchment Programme	16.0	8.0	0	23.9	0	-100.0
Use of Goods and Services	4 755.7	2 044.2	2 308.9	1 621.6	2 069.6	27.6
Interest Payments	2 020.8	924.2	863.9	1 508.6	1 010.0	-33.0
Grants and Other Payments	3 239.1	2 552.2	2 827.9	3 702.2	2 512.3	-32.1
Social Benefits	739.7	381.5	365.5	495.0	300.2	-39.3
Other Expenses	344.6	72.3	60.0	1 086.5	1 051.2	-3.3
Assets	9 139.9	5 465.7	3 353.7	7 736.3	3 284.9	-57.5
Non-Financial Assets	8 722.3	5 245.3	3 192.7	7 595.5	3 172.5	-58.2
Financial Assets	417.6	220.4	161.0	140.8	112.4	-20.2
Liabilities	413.9	225.9	156.0	504.0	264.6	-47.5
Changes in Balance	0	30.6	-167.1	2 669.3	-206.4	-107.7
Fiscal Balance: Surplus(+)/Deficit(-)	-5 413.9	-4 077.4	-4 150.4	-4 806.0	-3 192.9	-33.6
Financing	5 413.9	4 077.4	4 150.4	4 806.0	3 192.9	-33.6
Net Domestic Financing	1 863.5	1 306.7	2 394.1	1 843.1	3 554.6	92.9
Net External Financing	3 550.5	2 770.7	1 756.3	2 962.9	-361.7	-112.2

Source: Bank of Zambia

Table AIII.6: Sources of Reserve Money Growth

	Jan – June 2013		Jul –Dec 2013	
	Total (K'bn)	Contribution to Reserve Money Growth (%)	Total (K'bn)	Contribution to Reserve Money Growth (%)
1/ Net Foreign Assets (a+b+c+d)	638,280.2	489.6	781.1	63.6
a) Net Purchases from Govt	638,927.8		343.3	
b) Net Purchases from non-Government	-846.4		698.7	
c) Bank of Zambia own use of forex	0		0	
d) Change in stat. reserve deposits forex balances	198.7		-260.9	
2/ Net Domestic Assets (a+b)	-639,578.6	-490.6	446.9	36.4
a) Autonomous influences	-638,571.8		13,740.4	
Maturing Open Market Operations	616.0		12,388.5	
Direct Govt Transactions	-637,669.6		2,464.3	
TBs and Bonds Transactions	-1,510.7		-1,329.7	
Claims on non-banks (Net)	-7.5		217.3	
b) Discretionary influences	-1,006.8		-13,293.5	
Open Market Operations	-981.3		-13,247.2	
i. Short term loans	2,208.7		0	
ii. Repos/Outright TB sales	0		-1,349.0	
iii. Term Deposits Taken	-3,190.0		-11,898.2	
Treasury bill Rediscounts	0.0		0.0	
Other claims (Floats, Overdrafts)	-25.5		-46.3	
Change in Reserve Money (1+2)	-1,298.4		1,227.9	

Source: Bank of Zambia

Table AIII.7: Indicators of Bidding Behaviour in the Government Securities Market[1]

	Amts Offered (K blns)		Bid Amts (K blns)		Excess Demand (K blns)[2]		Subscription Rate (%)[3]	
	Jan – Jun, 13	Jul – Dec, 13	Jan – Jun, 13	Jul – Dec, 13	Jan – Jun, 13	Jul – Dec, 13	Jan – Jun, 13	Jul – Dec, 13
91-day bills	490.0	610.0	598.4	171.5	108.4	-438.5	122.1	28.1
182-day bills	1,240.0	1,660.0	2,244.5	1,558.3	1004.5	-101.7	181.0	93.9
273-day bills	1,340.0	1,880.0	1,780.4	1,600.7	440.4	-279.3	132.9	85.1
364-day bills	2,480.0	3,050.0	2,830.2	3,214.8	350.2	164.8	114.1	105.4
TOTAL	5,550.0	7,200.0	7,453.5	6,545.3	1,903.50	- 654.70		90.91
2-year bond	115.0	160.0	258.6	74.5	143.6	-85.5	134.30	46.6
3-year bond	330.0	500.0	539.4	569.1	209.4	69.1	224.9	113.8
5-year bond	520.0	700.0	538.2	507.0	18.2	-193.0	163.5	72.4
7-year bond	85.0	140.0	136.9	102.1	51.9	-37.9	103.5	72.9
10-year bond	180.0	260.0	183.7	107.0	3.7	-153.0	161.1	41.1
15-year bond	70.0	80.0	29.2	38.5	-40.8	-41.6	102.1	48.1
TOTAL	1,300.0	1,840.0	1,686.0	1,398.0	386.0	-442.0	41.7	76.0

Source: Bank of Zambia
1 Treasury bills were offered fortnightly while Government bonds are offered Quarterly.
2 Excess Demand = Amounts Bid less Amounts Offered, (-ve = shortfall, +ve = excess)
3 Subscription Rate = bid amounts as percentage of amount offered

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