Bank Of Zambia

Monetary Policy Statement

JUL - DEC 2016

Bank of Zambia

MISSION STATEMENT

The principal purpose of the Bank of Zambia is to "*achieve and maintain price and financial system stability to foster sustainable economic development*".

This Monetary Policy Statement is made pursuant to Part II, Section 9 of the Bank of Zambia Act Chapter 360 of the Laws of Zambia

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Executive Summary

This statement presents an economic outlook for the second half of 2016, outlines macroeconomic objectives for 2016 that will guide monetary policy implementation, and reviews the performance of monetary policy during the first half of 2016.

Global economic growth for 2016 is estimated at 3.1% and is expected to pick up to 3.4% in 2017, largely driven by emerging market and developing economies. However, downside risks remain, with the vote by the United Kingdom to withdrawal from the European Union (Brexit) expected to negatively impact on confidence and investment, and posing risks to the Euro Area and global economic growth.

On the domestic scene, Zambia's real GDP growth is projected to improve marginally in 2016, and more strongly in the medium-term. The coming on stream of new energy projects that are expected to add to the national grid will ease current electricity constraints and provide a stimulus to economic activity. Other sectors expected to drive growth include agriculture, mining, and accommodation and food services.

Inflation is projected to continue trending downwards in the second half of the year, declining to single digit by the end of the year. This outlook is premised on the effects of tight monetary policy implemented in November 2015 and relative stability in the exchange rate, which is expected to dampen imported inflation. In addition, the projected maize grain surplus from the 2015/16 farming season is expected to help stabilise food prices. However, the risks to this outlook include the regional maize grain shortage, the upward adjustment in the maize floor price, and the potential weakening of the exchange rate on account of continued weak global growth prospects are expected to exert pressure on domestic prices.

Monetary operations over the second half of 2016 will continue to focus on anchoring inflationary expectations in order to achieve the 2016 end-year inflation target of 7.7%. Therefore, the Bank of Zambia will maintain a tight monetary policy stance, while remaining mindful of the need to ensure that domestic economic activity is not severely constrained and that financial stability is maintained.

With regard to developments in the first half of 2016, the Bank of Zambia continued on a tight monetary policy path. The new forward looking monetary policy framework aimed to achieve single digit inflation over the medium-term. Monetary operations were aimed at maintaining the 5-day weighted average interbank rate within a corridor of +/- 2 percentage points of the Bank of Zambia (BoZ) Policy Rate, which was maintained at 15.5% during the review period.

However, monetary policy implementation in the first half of the year was faced with a number of challenges, which included the general rise in the cost of production, high food prices, and the continued rationing of electricity supply, which hampered productivity. These challenges may limit the attainment of the end-year inflation target of 7.7% announced in the 2016 Budget Address by the Hon. Minister of Finance.

Inflation rose to an average of 21.8% in the first half of 2016 against an average of 12.8% in the second half of 2015. The lagged pass-through effects from the depreciation of the Kwacha, high production costs and high maize grain prices contributed to higher prices during the review period. However, month-on-month changes moderated to levels consistent with single digit inflation after the first quarter of the year.

Liquidity conditions in the money market continued to be tight over the first half, and access to the overnight lending facility (OLF) continued to be limited to once a week. The average interbank rate traded above the upper bound of the BoZ Policy Rate corridor during the first quarter. However, the interbank rate fell sharply in the second quarter, slightly above the upper bound of the Policy Rate corridor as liquidity conditions improved on net Government spending.

Both broad money and domestic credit contracted, following tight monetary conditions. The contraction in broad money was driven by the reduction in gross international reserves while the decline in credit was mainly due to tight liquidity conditions and high lending rates.

Commercial banks' nominal interest rates generally trended upward following the rise in the cost of funds and tight liquidity conditions. Yield rates on Government securities also rose mainly due to tight liquidity conditions and investors' perception of increased government appetite for domestic borrowing. Similarly, the average interest rates in the NBFIs sector rose following the removal of interest rate caps by the Bank of Zambia in November 2015. However, real savings and deposit rates remained negative.

The trade deficit narrowed owing to a stronger contraction in the imports bill relative to the fall in exports. The fiscal deficit also narrowed in the first half of 2016, reflecting lower expenditures due to a large shortfall on external financing.

1 Introduction

This Monetary Policy Statement provides an outlook for global economic growth, domestic inflation projections and describes monetary policy objectives for the second half of 2016. The statement also reviews the performance of monetary policy during the first half of 2016. Selected macroeconomic indicators are presented in the appendix.

2 Global Economic Outlook: 2016 - 2017

2.1 Economic Growth[1]

The global economy is projected to grow at 3.1% and 3.4% in 2016 and 2017, respectively. Underlying this growth projection is largely emerging markets and developing economies, as Brazil and Russia show encouraging positive signs of recovery from deep recessions. Consumer demand and business confidence appear to have improved in Brazil, with the country's 2016 first quarter GDP contracting by a smaller margin than projected. It is expected that Brazil's growth will turn positive in 2017.

Downside risks to the euro area will weigh on global economic growth, driven largely by the Brexit effect, coupled with low crude oil prices due to high inventories. The Brexit effect may have significant medium-term implications for trade and investment flows particularly for the UK and the remaining EU countries, although the short-run effects could be limited.

Growth in Zambia's major trading partners is expected to slowdown in 2016 and 2017, attributed mainly to a lower projected growth in China. China's import volume growth is expected to continue softening as the overall economy is also anticipated to continue slowing. Further, the rebalancing of the economy from external to domestic demand, and from investment to consumption, will continue to weigh down on commodity import volumes.

In South Africa, growth is expected to remain fragile in the short to medium-term mainly due to political and policy uncertainties alongside heightened global financial volatility and weak Chinese demand. The IMF downgraded South Africa's growth forecast to 0.1% in 2016 from an earlier 0.6% with growth for 2017 projected at 1.1%. Other risks to economic growth in South Africa relate to the UK referendum decision to leave the EU, electricity and water supply constraints coupled with a weak currency which may also dampen growth prospects. The Democratic Republic of Congo (DRC) growth prospects continue to be affected by low prices for its main export commodities and political uncertainty which has been adversely affecting the business environment. Growth is projected at 5.1% in 2016, down from 6.9% in 2015. The balance of payments deficit is also projected to widen in 2016 while gross international reserves are expected to continue to decline.

The uncertain global economic outlook, with weaker growth prospects, particularly in Zambia's main trading partners, and heightened uncertainties in emerging and advanced economies, pose some risks to Zambia's external outlook and inflation in 2016. Zambia's current account will remain under pressure in 2016 as the economy continues to face challenges from subdued price and low demand for copper by China as well as the decline in earnings from non-traditional exports, especially to the DRC.

2.2 Commodity Prices

The forecast for the rest of 2016 indicates an increase in crude oil prices, attributed to disruptions in supply and strong demand. This development is expected to move the market into a small deficit in the second half of the year owing to continued declines in non-OPEC supply and limited gains in OPEC production, thereby allowing for a modest reduction in stocks.

Metal prices, however, are expected to remain subdued in 2016, mainly on account of an anticipated continued copper surplus and weak growth prospects in emerging market and developing economies. However, metal prices are expected to record some gains in 2017 owing to Chinese stimulus programme directed towards the construction sector.

The prices of agricultural commodities are expected to increase slightly in 2016 due to unfavourable weather patterns in South America, but are still expected to register a marginal decline relative to 2015. Food prices are projected to increase in 2016, and to remain broadly unchanged in 2017 on account of changing weather conditions.

3 Domestic Economic Outlook for 2016 – 2017

Challenges in the domestic economy emanating from weak copper prices, and high production costs (i.e. high lending rates and effects of power rationing), are expected to continue to constrain growth in 2016.

[1]Global growth projections from IMF World Economic Outlook July 2016 Update

However, over the medium-term, the outlook is more optimistic. GDP growth is projected to improve marginally in 2016 to 3.0% from 2.9% in 2015. However, this growth remains significantly below the average growth rate registered over the past decade.

The Government has outlined a number of measures to accelerate the pace of economic diversification with emphasis on agriculture, industrialisation and tourism. The country remains attractive to foreign investment, evidenced by a number of new projects around the country. Thus, investment in some non-mining sectors, such as agriculture, tourism and energy, are expected to drive growth over the medium-term.

In the agriculture sector, results from the 2015/2016 Crop Forecast Survey indicate a 9.7% increase in maize output, estimated at 2,873,052 MT. The sector is expected to continue recovering as weather conditions improve. In the medium-term, the coming on stream of new energy projects that will add to the national grid is expected to provide stimulus to economic activity across all sectors. Growth in the accommodation and food services sector is also projected to be positive, supported by the hosting of a number of international events such as the African Development Bank (AfDB) annual conference and the Inter-Parliamentary Union conference.

In 2017, the outlook for growth is more optimistic as GDP is expected to grow at around 3.4%. Growth is expected to emanate from new mining projects as they come on stream, improved agriculture production following the forecast for normal rainfall influenced by the La Niña over the 2016/17 rainy season, and improved manufacturing output as electricity supply improves. In addition, the anticipated improvement in electricity generation is expected to boost growth in the energy sector while the continued investment in infrastructure is expected to yield positive effects in the construction and tourism sectors.

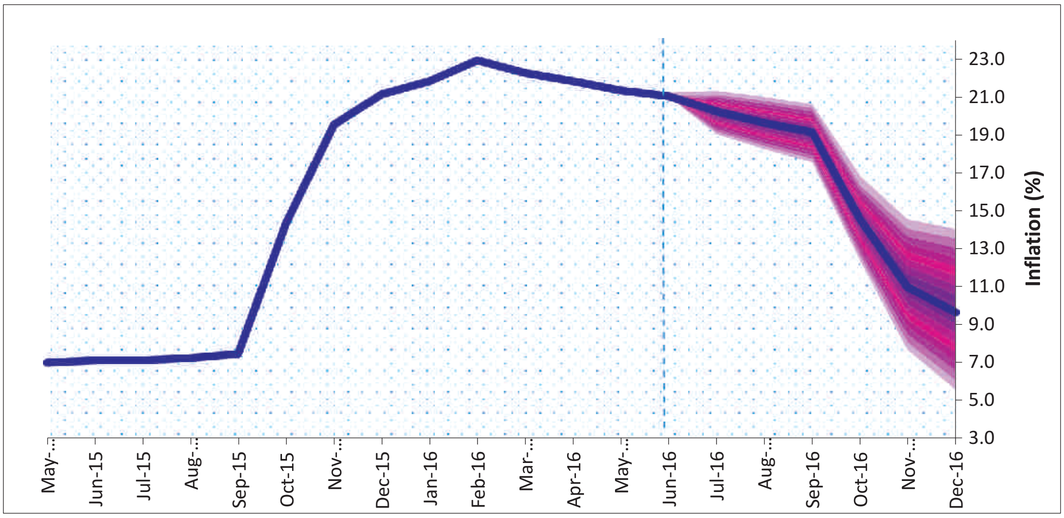
4 Inflation Projections for the Second Half of 2016[2]

Inflation is projected to continue trending downwards in the second half of 2016, declining to an average of 15.2% from the actual average outturn of 21.8% in the first half of the year (Chart 1 and Table 1 - Appendix). At end-December 2016, inflation is projected to decline to 9.4% from 21.0% in June 2016.

The slowdown in inflation is expected to emanate mainly from relative stability in the exchange rate and the effects of continued tight monetary policy. The estimated maize grain surplus from the 2015/2016 farming season is also expected to contribute to the relative stability in domestic prices of maize grain and products, thereby help moderate food inflation.

However, there are risks and uncertainty to the inflation projection in the second half of 2016. Key risks include the regional maize grain shortage. This is expected to keep prices of maize grain and products at elevated levels, thereby limiting the extent of the reduction in domestic food prices. The upward adjustment in the maize floor price from K75 to K85 per 50 Kilogramme (Kg) bag coupled with the private sector's purchase of maize grain at around K100 per 50 Kg is also expected to result in relatively higher prices for maize grain and other related products, particularly during the lean period of October to December 2016. In addition, the potential weakening of the Kwacha against the US dollar on account of increased demand for foreign exchange as businesses stock up imported goods in readiness for the festive season, should it materialise, is likely to exert upward pressure on inflation.

Chart 1: Actual and Projected Inflation: Jan 2015 – Dec 2016



Source: Bank of Zambia /Central Statistical Office

5 Monetary Policy Objectives and Instruments for the Second Half of 2016

Monetary operations over the second half of 2016 will continue to focus on anchoring inflation expectations in single digits over the medium-term, with the immediate end-year target of 7.7% set. Annual inflation is projected to be on a downward trend over the second half, with monthly changes in inflation expected to drop to levels that are consistent with single digit inflation.

Consistent with this objective, the Bank of Zambia will maintain a tight monetary policy stance and continue to use market-based instruments of monetary policy to realign market interest rates to the Policy Rate. The Bank of Zambia will remain mindful of the need to ensure that domestic economic activity is not severely constrained, and that financial stability is maintained. With regard to the exchange rate, the Bank of Zambia will continue to maintain a market driven exchange rate in tandem with other macroeconomic objectives.

Monetary policy formulation and implementation will also continue to support Government's broader macroeconomic objectives (Table 2 - Appendix) outlined in the MTEF 2016-2018. These include:

i. Achieving a real GDP growth rate of at least 3.4% in 2016;

ii. Achieving an end-year inflation rate of no more than 7.7% in 2016;

iii. Containing domestic borrowing to no more than 1.2% in 2016; and

iv. Increasing international reserves to at least 4 months of import cover.

6 Review of Global Developments in the First Half of 2016

6.1 Economic Growth

Global economic growth remained subdued in the first half of 2016 as downside risks persisted. In the U.S., growth was supported by consumer spending, which remained the main driver of economic activity. Labour market conditions continued to improve, with the unemployment rate stabilising around 5.0%. However, the economy continued to be affected by the decline in exports mainly as a result of weak economic conditions in the main trading partner countries and a relatively strong U.S. dollar. In the Euro area, economic growth remained positive as energy prices declined and labour market conditions continued to improve, thus boosting private consumption. Economic growth also benefited from relatively robust growth in investment and public sector expenditure.

Economic conditions remained weak in the largest emerging market economies, although a modest rise in commodity prices in the second quarter of 2016 stimulated growth in net commodity exporting economies. India and the rest of the emerging Asia continued to grow at a robust pace, although some countries faced some spill over effects of China's economic rebalancing and global manufacturing weakness.

Most of the countries in the Sub-Saharan African region continued to face multiple shocks, including low commodity prices, tighter financial conditions and shortages of food due to adverse weather conditions, particularly in Eastern and Southern Africa. The fall in commodity prices in the earlier part of the year continued to put severe strain on the fiscal and external sector of most economies, including Zambia. Further, weather patterns caused by the El Niño phenomenon caused substantial fluctuations in food prices and inflation across the continent, thus impacting on growth prospects.

The weaker global economic conditions negatively affected economic growth of Zambia's main trading partners such as China and South Africa. In China, economic growth continued to slow down on the back of weaker investment growth as the economy continues to shift away from manufacturing to consumption. In South Africa, growth continued to be negatively affected by weak demand from China, a weaker currency and political uncertainty which affected business and investor confidence.

6.2 Commodity Prices

Copper prices decreased to US$4,733/mt in June 2016 from US$4,885/mt in December 2015 as China's demand for the commodity continued to be weak. On the other hand, crude oil prices increased to US$42.9/barrel in June 2016 from US$41.2/barrel in December 2015. The increase in prices was largely explained by a fall in oil extraction in the United States and supply disruptions in some major oil-producing countries (Nigeria, Kuwait, Canada, Venezuela and Libya), coupled with the brighter outlook for economic growth in emerging market economies.

The prices of most agricultural products increased. For example, prices of cotton increased to US$1.6/kg from US$1.5/kg while prices for sugar rose to US$0.4/kg in June 2016 from US$0.3/kg in December 2015. Prices of soybeans similarly increased to US$424/mt from US$372/mt over the same period. However, wheat prices fell to US$177.7/mt from US$179.6/mt while prices of maize decreased to US$171.1/mt in June 2016 from US$176.2/mt in December 2015.

7 Review of Domestic Developments in the First Half of 2016

7.1 Assessment of Monetary Policy Implementation

The Bank of Zambia is transitioning to a forward looking monetary policy framework. Monetary policy during the first half of 2016 was focused on achieving single digit inflation over the medium-term, with the immediate end year target for end-2016 set at 7.7%. With regard to monetary operations, the Bank of Zambia had allowed the interbank interest rate to remain above the Policy Rate corridor following the tightening in monetary policy in November 2015. This was largely to assist in stemming volatility in the foreign exchange market experienced in the last half of 2015. As the first half progressed, the Bank of Zambia was committed to allowing the interbank interest rate to gradually revert towards the Policy Rate corridor.

The BoZ Policy Rate remained unchanged at 15.5% throughout the review period on account of tight monetary policy measures taken in November 2015 which were already producing desired results. The Bank of Zambia also continued to restrict access to the Overnight Lending Facility window to only once a week, except where express permission was granted. As a result, the exchange rate remained relatively stable and annual inflation that peaked in the first quarter slowed down in the second quarter.

7.2 Challenges to Monetary Policy Implementation

The implementation of monetary policy during the first half of 2016 was faced with a number of challenges which are likely to constrain the attainment of the end-year inflation target of 7.7%.

The unfavourable global economic environment continued to dampen demand for export commodities resulting in low copper prices, which in turn negatively affected the performance of the external sector. The deficit of maize grain in the region kept domestic prices elevated during the first half, translating into higher food inflation. Although the exchange rate of the Kwacha against the US dollar was relatively stable during the first half of the year, the general rise in production costs, electricity rationing and the high cost of credit continued to adversely affect productivity in the economy and subsequently the prices of goods and services. Preliminary data indicate a slowdown in GDP growth in the first quarter of 2016. The economy grew by 3.1% year-on-year, slightly slower than the 3.9% growth recorded in the corresponding period in 2015. The Composite Index of Economic Activity[3] (CIEA) and survey data on business opinion and expectations indicate a general reduction in economic activity in the first half of the year. The flow of credit to the private sector has continued to contract largely due to high lending rates and tight liquidity conditions and crowding out of the private sector through high Government borrowing requirements. This has restricted business investment spending and private consumption. The high budget deficits in recent years continue to adversely impact on the ability of monetary policy to achieve its objectives.

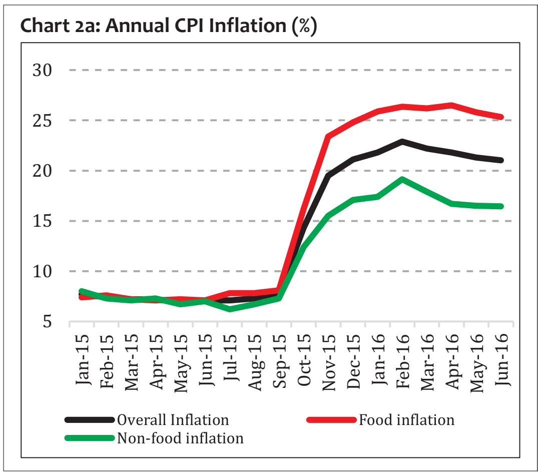
7.3 Inflation and Market Developments

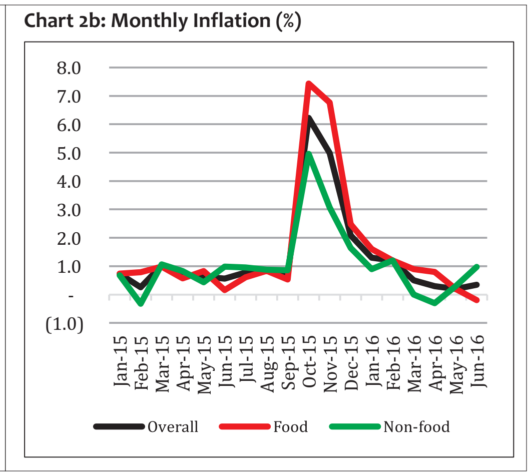
Inflation Outturn

Annual overall inflation was projected to average 21.6% in the first half of 2016, up from the average outturn of 12.8% during the second half of 2015. The projected higher inflation was mainly on account of the lagged pass-through effects from the sharp depreciation of the exchange rate in the second half of 2015, which contributed to higher inflation in the last quarter of the year. High food prices, induced by high maize grain prices, and high production costs partly attributed to electricity rationing were also expected to contribute to inflationary pressures during the first half of 2016. The tightening of monetary policy in the fourth quarter of 2015 was expected to contribute to relative stability in the exchange rate and anchor inflation expectations, thereby moderating inflationary pressures during the first half of 2016. In general, the risks to inflation were judged to be on the upside during the first half of 2016.

The overall annual inflation rate accelerated to an average of 21.8% in the first half of 2016 from an average of 12.8% in the last half of 2015. Inflation ended the period at 21.0% in June 2016 from 21.1% in December 2015 (Chart 2a). Both food and non-food inflation rates rose to averages of 26.0% and 17.4% during the review period from averages of 14.7% and 10.8% in the preceding period, respectively. The lagged pass-through effect from the depreciation of the Kwacha exchange rate, high production costs and high maize grain prices contributed to higher prices during the review period. However, month-on-month overall inflation also declined to 0.3% in June 2016 from 2.1% in December 2015 (Chart 2b).

[3]The CIEA is an indicator developed by the Bank to provide an aggregate measure of the current state of economic activity and their direction over time.





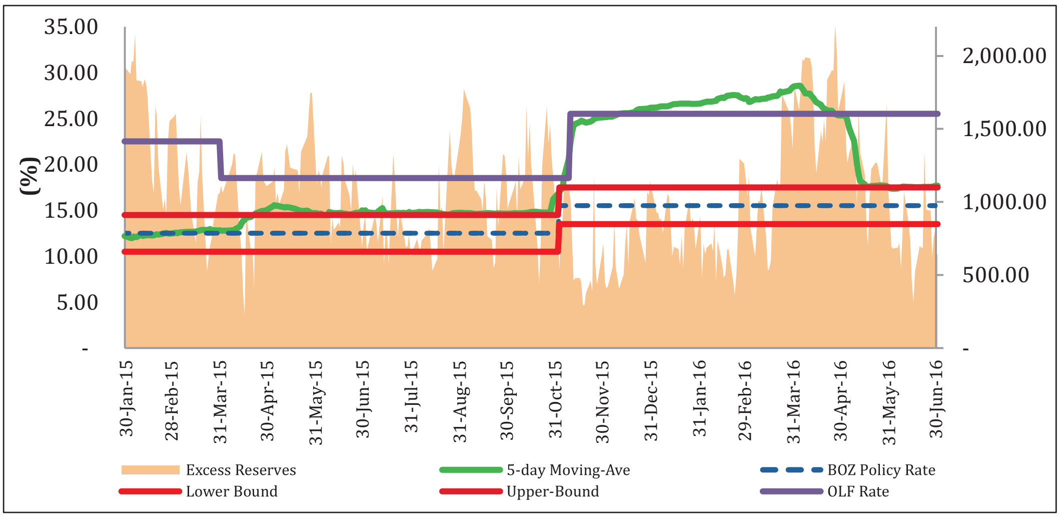
Source: Central Statistical Office

Money Market Liquidity and Interbank Trading

Market liquidity, as measured by the aggregated current account balance of banks, decreased by 28.8% to close the period at K0.8 billion (Chart 3 and Table 3 - Appendix). The decrease in liquidity levels was mainly due to net Government revenue and statutory reserve transfers.

As liquidity levels dropped and the funds remained concentrated in a few banks, the demand for overnight interbank funds rose by 14.1% to K97.3 billion. Correspondingly, the interbank rate rose to an average of 22.6% from 17.7% recorded in the last half of 2015. However, as liquidity conditions improved in the second quarter due to net Government spending, the interbank rate declined sharply and ended the quarter slightly above the upper bound of the Policy Rate corridor of 17.5% (Chart 3).

Chart 3: Market Liquidity an Interbank Rate



Source: Bank of Zambia

Government Securities Market

The demand for Government securities remained generally low as liquidity conditions remained tight. Negative sentiments arising from the weak global growth outlook also weighed on the demand for emerging market assets as non-resident investors unwound their positions in preference for safe havens. Consequently, a total of K5.9 billion was raised from Government securities (at cost) compared to K6.1 billion in the last half of 2015. A total of K4.9 billion (at cost) was raised through Treasury bills (K5.2 billion in the last half of 2015) while K0.94 billion was raised through bonds, slightly up from K0.92 billion previously.

Foreign Exchange Market

The rate of depreciation of the Kwacha against currencies of major trading partner countries moderated in the first half of 2016. The Kwacha depreciated by 5.0% against the US dollar to an average of K10.7140 per US dollar compared to the sharp depreciation of 43.7% in the last half of 2015 (Table 4 –

Appendix). Accounting for the slowdown in the rate of depreciation was mainly the effects of the tight monetary policy measures implemented by Bank of Zambia in the fourth quarter 2015 that limited the supply of Kwacha liquidity on the money market and also raised the cost of credit to support demand for foreign exchange.

On a trade-weighted basis, the Kwacha appreciated by 1.1% in real terms. This is reflected in the decline in the real effective exchange rate index to 118.6 in June 2016 from 120.0 in December 2015, attributed mostly to the rise in domestic inflation relative to trading partner countries (Table 5 - Appendix).

Capital Markets

Trading activity at the Lusaka Securities Exchange Plc. declined. Market capitalisation fell by 6.0% to K60.3 billion in June 2016, while the All-share Index declined by 17.0% to 4,753.3 at end-June 2016. The fall in capital market activity was largely attributed to the decline in share prices of some companies on account of market competition, delays in declaring dividends, and reported losses.

Interest Rates

Interest rates continued to rise in the first half of 2016 as monetary conditions remained tight and financial institutions adjusted with a lag to the removal of interest rate caps in November 2015. Yield rates on both Treasury Bills and Government Bonds edged upward by 5.1 and 2.8 percentage points to 24.6% and 25.4%, respectively (Table 5 – Appendix). Investors' perception of higher Government appetite for borrowing following the increase in tender sizes in the first half of the year contributed to rise in yield rates.

The funding cost by banks remained high as tight liquidity conditions persisted, and contributed to elevated lending rates. The average 180-day deposit rate for amounts exceeding K20, 000 rose to 12.4% from 10.5% (Table 5 - Appendix). The cost of credit in the non-bank financial institutions' sector (average effective annual interest rate) increased to 38.8% from 37.7% in the second half of 2015 (Table 6 - Appendix) following the removal of interest rate caps by the Bank of Zambia in November 2015 and the general rise in the cost of doing business. Consequently, lending rates edged upward to 27.1% from 21.7% during the period under review (Table 5 - Appendix).

Broad Money

Broad money (M3) contracted by 6.6% in the first half of 2016 to K44.1 billion compared to the growth of 28.2% in the second half of 2015 (Table 7 - Appendix). The decline in M3 was driven by the reduction in gross international reserves, mainly attributed to external debt service and crude oil payments. On an annual basis, M3 growth slowed down to 19.7% in June 2016 from 35.2% in December 2015.

Domestic Credit

Domestic credit contracted by 3.1% to K46.1 billion in the first half of 2016 against the growth of 7.5% recorded during the second half of 2015 (Table 8 - Appendix). Foreign currency loans shrunk by 9.2% compared to a growth of 42.0% recorded the second half of last year, reflection mainly revaluation effects following the appreciation of the Kwacha. The Kwacha denominated credit also contracted by 1.5% against the growth of 1.1% recorded during the second half of 2015. Domestic credit slowed mainly on account of high lending rates and general tight liquidity in the market. The household (personal loans) category continued to account for the largest share representing 27.3% (29.0% in Dec 2015) followed by agriculture, forestry and fishing sector at 17.4% (17.3% in Dec 2015) as shown in Table 9 – Appendix.

International Trade[4]

The trade deficit narrowed to US$290.4 million from US$743.2 million due to a strong contraction in imports than exports (Tables 10 and 11 - Appendix).

Merchandise imports fell by 23.2% to US$3.4 billion in the first half of 2016, with reductions occurring across all major items, except electrical and machinery equipment. The broad fall in imports may be attributed to the sharp depreciation of the Kwacha in the second half of 2015 that curtailed demand.

Export earnings reduced by 15.6% to US$3.1 billion in the first half of 2016, largely attributed to a 20.1% reduction in copper export earnings to US$2.1 billion (Table 12 - Appendix). This reflects the fall in both export volumes and realised prices. Copper export volumes, at 463,290.1 metric tonnes (mt),

[4]Export volumes refer to gross volumes exported which include, but not restricted to production from Zambian mines.

were 16.8% lower and the average realized price recorded a 4.0% reduction, averaging US$4,530.6 per mt. Likewise, non-traditional export earnings (NTEs) fell by 7.2% to US$874.9 million, on account of declines in gemstones, sulphuric acid and cane sugar earnings.

Gross international reserves stood at US$2.4 billion at end-June 2016, representing 3.7 months of import cover.

Fiscal Balance

The fiscal deficit (on cash basis) in the first half of 2016, at K1.6 billion, was lower than programmed (K5.0 billion) as shown in Table 13 - Appendix. This largely reflects lower spending on capital projects, mostly road infrastructure, due to a large shortfall on external financing. However, revenue performance was stronger by 10.8%, at K22.2 billion, against programmed revenues of K20.1 billion. This was attributed to over performance on non-tax revenue mostly relating to dividend payments by state owned institutions.

8 Conclusion

Although inflation remained high, inflationary pressures moderated in the first half of the year compared to the last half of 2015. Inflationary pressures are expected to moderate further in the second half of the year, as food supply improves following the commencement of the harvest period and the base effect[5] are removed in the last quarter of 2016.

The measures undertaken by the Bank of Zambia to tighten monetary policy in November 2015 have been effective in stabilising the exchange rate which has contributed to the slowdown in inflation in the first half of 2016. Month-on-month, inflation has decelerated to levels consistent with single digit inflation. As base effects phase off, annual inflation is expected to fall back to single digits by the end of the last quarter of 2016.

However, challenges on the supply side of the economy remain, which threaten the effectiveness of monetary policy in containing inflation. Although power supply is expected to improve, the high cost of production, high lending rates, and increased cost of imported intermediate inputs may continue to hamper productivity and production in the economy.

Developments in the global economic environment continue to present a significant challenge to our external sector performance. In this regard, the main strategy remains that of diversifying the economy and promoting export growth.

The Bank of Zambia, therefore, remains committed to maintaining macroeconomic stability and will continue to implement prudent monetary policies to support and promote economic growth. A stable macroeconomic environment will generally be associated with low and stable inflation, lower interest rates, which in turn will encourage households and businesses to borrow for investment purposes, thereby boosting production levels and building a more resilient economy. In view of this, the Bank of Zambia will ensure that tight monetary conditions do not weaken growth prospects and impose constraints on financial sector growth, with potentially adverse effects on financial system stability.

[5]The base effect in this case relates to the upward shift in the consumer price index following a significant depreciation in the exchange rate in September 2015

Appendix

Table 1: Actual and Projected Inflation: Jan 2015 – Dec 2016

	Projection (a)	Actual (b)	Forecast Error (b-a)
Jan 2015	8.0	7.7	-0.3
February	7.8	7.4	-0.4
March	7.6	7.2	-0.4
April	7.3	7.2	-0.1
May	7.2	6.9	-0.3
June	7.1	7.1	0.0
July	7.2	7.1	-0.1
August	7.2	7.3	0.1
September	7.5	7.7	0.2
October	7.9	14.3	6.4
November	19.9	19.5	-0.4
December	20.3	21.1	0.8
Jan 2016	21.9	21.8	-0.1
February	21.7	22.9	1.2
March	21.5	22.2	0.7
April	21.6	21.8	0.2
May	21.2	21.3	0.1
June	21.5	21.0	-0.5
July	20.3	20.2	-0.1
August	19.8	19.6	-0.2
September	19.2	18.9	-0.3
October	13.9	12.5	-1.4
November	9.8	8.8	-1.0
December	9.4		

Source: Bank of Zambia/ Central Statistical Office

Table 2: Macroeconomic Outturn and Targets: 2015 and 2016

	2015 Target	2015 Outturn	2016 Target
Real GDP growth rate (%)	7.0	2.9	3.4
CPI Inflation, end period (%)	7.0	21.1	7.7
Gross Official Reserves (months of imports)	4.0	3.7	4.0
Broad Money growth (%)	15.2	35.2	18.0
Budget deficit (on cash basis, excluding grants), % of GDP	4.6	8.1	3.9
Domestic financing of Budget (% of GDP)	2.0	1.9	1.2

Source: Bank of Zambia, Central Statistical Office, Ministry of Finance

Table 3: Liquidity Influences (K' billion): 2014 – 2016

	Jul-Dec 2014	Jan-Jun 2015	Jul-Dec 2015	Jan-Jun 2016
Opening balance	0.8	2.4	0.7	1.1
Net Government spending	4.8	1.6	4.4	-1.3
BoZ foreign exchange influence	-0.9	-1.4	-6.3	-0.1
BoZ operations	-1.4	-1.5	-3.9	-1.8
change in currency in circulation	-0.7	0.6	-1.0	0.1
change in SR deposits	-0.4	-2.2	-2.0	-1.7
Overnight Lending Facility	-0.2	0.1	-7.7	-0.2
Net Government securities influence	-0.3	-1.7	3.5	1.6
Open market operations	0.0	0.0	0.2	-0.3
Closing balance	2.4	0.7	1.1	0.8

Source: Bank of Zambia
SR=statutory reserve

Table 4: Exchange Rate: Jun 2014 – Jun 2016

Bilateral Nominal Exchange Rate (period average)					
	Jan-Jun 2014	Jul-Dec 2014	Jan-Jun 2015	Jul-Dec 2015	Jan-Jun 2016
USD/ZMW	6.0652	6.2362	7.1010	10.2021	10.7140
GBP/ZMW	10.1258	10.1381	10.8221	15.6168	15.3506
EUR/ZMW	8.3125	8.0241	7.9151	11.2504	11.9499
ZAR/ZMW	0.5669	0.5677	0.5951	0.7461	0.6943
Real Trade-weighted Exchange Rate (end-period)					
	Jun 2014	Dec 2014	Jun 2015	Dec 2015	Jun 2016
Domestic CPI (2005=100)	209.7	215.9	224.7	261.4	271.7
Weighted Foreign CPI (2005=100)	129.7	130.2	130.9	132.6	137.1
NEER Index (2005=100)	2.23	2.07	2.33	3.09	3.07
REER Index (2005=100)	105.8	95.9	105.0	120.0	118.6

Source: Bank of Zambia

Table 5: Interest Rates (%, period average): 2014 – 2016

	2014	2015		2016
	Second Half	First Half	Second Half	First Half
BoZ Policy Rate (end-period)	12.5	12.5	15.5	15.5
Overnight Lending Facility rate (end-period)	22.1	20.5	20.0	25.5
Overnight interbank rate	13.6	13.4	17.7	24.3
Average commercial banks' lending rate	19.8	20.4	21.7	27.1
Savings rate	3.1	2.9	2.9	3.0
more than K100	3.5	3.4	3.4	3.3
above K20,000 (180 days)	9.8	10.5	10.5	12.4
Treasury bill yield rates				
composite yield rate	16.4	18.5	19.5	24.6
91days	10.4	13.6	15.0	21.6
182 days	17.4	18.8	19.9	24.4
273 days	17.4	19.4	20.8	26.3
364 days	20.4	22.1	22.5	26.3
Government bond yield rates				
composite yield rate	18.2	20.3	22.6	25.4
2 years	15.4	15.4	20.8	24.5
3 years	16.2	18.1	23.2	24.3
5 years	19.1	23.1	25.5	28.3
7 years	19.3	21.4	23.6	28.5
10 years	19.5	21.7	20.3	23.4
15 years	19.9	22.5	22.5	23.5

Source: Bank of Zambia

Table 6: Average Annual Non-Banks' Effective Interest Rates (%): 2015 and 2016

	Second Half 2015	First Half 2016
Microfinance Institutions	56.1	53.9
Leasing Finance Institutions	34.4	54.9
Building Societies	34.3	41.8
Development Bank of Zambia	27.0	27.6
National Savings and Credit Bank	36.5	36.5
Financial Businesses	0.0	17.8
Overall for the sector	37.7	38.8

Source: Bank of Zambia

Table 7: Broad Money (K' billion unless otherwise stated): Jun 2014 – Jun 2016

	Jun 2014	Dec 2014	Jun 2015	Dec 2015	Jun 2016
Broad Money (M3)	32.7	35.0	36.7	47.3	44.1
Foreign Exchange (FX) Deposits	10.0	9.9	12.2	20.8	18.4
M3 (excl. Foreign Exchange Deposits)	22.7	25.0	24.7	26.5	25.8
6-month change in M3 (%)	5.0	7.0	5.4	28.2	-6.6
6-month % change in Forex deposits	30.9	-0.5	22.3	70.8	-11.5
6-Month % change in M3 (excl. Forex deposits)	-3.4	10.2	-1.3	7.3	-2.8
Annual % change in M3 (%)	17.6	12.3	12.8	28.2	19.7
Annual % change in Forex deposits	35.4	30.3	21.7	108.2	51.2
Annual % change in M3 (excl. Forex Deposits)	10.7	6.4	8.8	3.5	4.2

Source: Bank of Zambia

Table 8: Domestic Credit (K' billion unless otherwise stated): Jun 2014 – Jun 2016

	Jun 2014	Dec 2014	Jun 2015	Dec 2015	Jun 2016
Domestic Credit (DC)	37.5	39.3	44.3	47.6	46.1
o/w foreign currency denominated	5.5	7.0	6.9	9.8	8.9
DC (excl. FX denominated credit)	32.0	32.3	37.4	37.8	37.2
6-month % change in DC	6.2	4.8	12.7	7.5	-3.1
6-month % change in Forex Credit	-34.9	27.3	-1.4	42.0	-9.2
6-Month Change in DC (Excl. Forex Credit)	19.1	0.9	15.8	1.1	-1.5
Annual Change in Domestic Credit	15.2	11.2	18.2	21.2	4.1

Source: Bank of Zambia

Table 9: Shares of Total Loans and Advances by Sector (%): Jun 2014 – Jun 2016

	Jun-14	Dec-14	Jun-15	Dec-15	Jun 2016
Agric, forestry, fishing & hunting	17.6	16.6	16.3	17.3	17.4
Mining & Quarrying	5.8	5.0	5.0	6.4	5.6
Manufacturing	10.5	11.5	11.4	13.5	12.4
Electricity, Gas, Water & Energy	1.9	2.2	1.6	1.7	1.5
Construction	3.2	3.4	3.0	3.4	3.8
Wholesale & Retail Trade	9.3	7.8	9.6	10.8	10.7
Restaurants & Hotels	1.8	1.6	1.5	1.6	1.5
Transport, Storage & Communications	5.0	5.6	5.4	5.1	5.2
Financial Services	2.0	2.5	2.7	2.7	2.8
Community, Social & Personal	2.9	2.1	1.9	1.7	2.1
Real Estate	3.0	2.3	2.6	2.9	3.0
Personal Loans	34.5	34.9	33.2	29.0	27.3
Others	2.4	4.5	5.7	4.0	6.7

Source: Bank of Zambia

Table 10: Trade Data (c.i.f - US$ million): Jun 2014 – Jun 2016

	Jun-Dec 2014	Jan-Jun 2015	Jul-Dec 2015	Jan-Jun 2016
Trade Balance	273.3	-231.7	-743.2	-290.4
Total Exports, c.i.f. (including Gold)	5,200.1	3,615.4	3,690.2	3,116.0
General Exports, c.i.f.	5,135.9	3,547.7	3,605.2	3,016.5
Metals	3,977.9	2,642.1	2,662.2	2,141.6
Copper	3,914.5	2,605.6	2,628.1	2,099.0
Cobalt	63.4	36.5	34.2	42.6
Non -Traditional Exports	1,158.0	905.6	942.9	874.9
Exporter Audit Adjustor	-13.2	-13.2	-13.2	-13.2
Sub Total	1,171.2	918.8	956.1	888.0
Gemstones	86.9	44.6	66.6	54.4
Sulphuric acid	109.5	32.1	25.2	18.4
Industrial Boilers and Equipment	73.5	48.7	46.9	72.5
Cane Sugar	123.2	72.1	74.5	54.4
Gasoil/Petroleum Oils	11.5	8.3	3.9	3.9
Cement & Lime	49.2	34.9	30.3	31.1
Electricity	36.6	39.0	0.0	0.0
Raw hides, Skins & Leather	7.5	5.7	6.8	9.2
Sulphur, sublimed or precipitated; colloidal	23.7	15.0	4.6	2.0
Burley Tobacco	93.8	38.5	67.9	34.0
Copper Wire	43.4	34.3	24.3	33.1
Scrap of precious metals	30.0	25.0	24.1	0.0
Maize & Maize Seed	35.3	72.0	143.9	78.8
Electrical Cables	27.3	10.2	10.5	6.6
Cotton Lint	46.4	8.2	45.9	15.4
Soap, Active Agents, Washing Preps etc	51.7	24.6	26.9	16.2
Fresh Fruits & Vegetables	7.8	5.6	6.9	4.3
Manganese Ores/Concentrates	1.8	1.3	0.1	0.3
Wheat & Meslin	8.6	6.7	5.4	3.5
Fresh Flowers	5.3	8.6	4.7	4.5
Other	295.8	383.4	336.6	445.3
Gold	64.2	67.7	85.0	99.5
Imports c.i.f./1	-4,926.8	-3,847.1	-4,433.4	-3,406.4

Source: Bank of Zambia

Table 11: Imports by Commodity Groups (c.i.f - US$ million): Jun 2014 – Jun 2016

	Jun-Dec 2014	Jan-Jun 2015	Jun-Dec 2015	Jan-Jun 2016	% Change
Food Items	253.6	243.2	251.6	210.6	-16.3
Petroleum Products	773.3	560.6	975.8	697.8	-28.5
Fertilizer	175.9	155.9	205.5	105.5	-48.7
Chemicals	403.3	428.1	611.1	440.7	-27.9
Plastic and Rubber Products	222.3	190.4	173.3	139.6	-19.4
Paper and paper products	69.9	64.8	57.8	47.0	-18.8
Iron and Steel and items thereof	353.6	302.3	225.1	146.9	-34.8
Industrial Boilers and Equipment	768.3	639.0	588.2	452.3	-23.1
Electrical Machinery & Equipment	437.9	282.6	258.4	365.3	41.4
Vehicles	430.7	271.2	272.5	233.4	-14.3
Other Imports	1,037.9	709.2	814.1	567.3	-30.3
Total	4,926.8	3,847.1	4,433.4	3406.4	-23.2

Source: Bank of Zambia

Table 12: Metal Export Volumes, Values and Prices: Jun 2014 – Jun 2016

	Copper				Cobalt			
	Export Volumes (MT)	Export US $'000	Price/ Tonne	Price/ Pound	Export Volumes (MT)	Export US $'000	Price/ Tonne	Price/ Pound
Quarter 3	292,302.2	1,978,838.4	6,769.8	3.1	1,999.0	33,154.8	27,652.1	12.5
Quarter 4	296,559.1	1,935,638.7	6,527.0	3.0	1,089.0	30,234.7	27,763.7	12.6
Jun-Dec 2014	588,861.2	3,914,477.1	6,647.5	3.0	2,288.0	63,389.5	27,705.2	12.6
Quarter 1	232,587.5	1,277,217.6	5,491.3	2.5	990.0	26,090.6	26,345.1	12.0
Quarter 2	232,660.9	1,328,336.3	5,709.3	2.6	396.8	10,426.7	26,278.6	11.9
Jan-Jun 2015	465,248.3	2,605,553.8	5,600.4	2.5	1,386.8	36,517.3	26,332.5	11.9
Quarter 3	275,944.6	1,374,487.0	4,981.0	2.3	573.0	14,288.4	24,936.1	11.3
Quarter 4	280,905.5	1,253,574.2	4,462.7	2.0	1,019.0	19,899.4	19,528.4	8.9
Jun-Dec 2015	556,848.2	2,628,061.2	4,719.5	2.1	1,592.0	34,187.8	21,474.7	9.7
Quarter 1	237,636.6	1,043,080.2	4,389.4	2.0	1,241.2	22,037.1	17,754.4	8.1
Quarter 2	225,653.5	1,055,918.3	4,679.4	2.1	1,102.8	20,587.8	18,668.9	8.5
Jan–Jun 2016	463,290.1	2,098,998.5	4,530.6	2.1	2,344.0	42,624.9	18,184.6	8.2

Source: Bank of Zambia

Table 13: Central Government Fiscal Operations: 2016

	Proj (Kbln)	% of GDP	Target (Kbln)	Prel (Kbln)
Total Revenue & Grants	42.7	20.7	20.1	22.2
Tax Revenue	30.4	14.8	14.6	13.6
Non-Tax Revenue	11.7	5.7	5.3	8.3
Grants	0.5	0.3	273	0.3
Total Expenditure	53.1	23.8	26.0	23.9
Current Expenditure	40.5	19.7	20.1	20.9
Personal Emoluments	20.4	9.9	9.8	9.2
Use of Goods & Services	5.0	2.4	2.1	2.1
Interest	7.1	3.4	3.5	3.6
Grants & Other Payments	6.1	3.0	3.7	5.5
Social Benefits	1.1	0.5	0.6	0.2
Other Expenses	0.8	0.4	0.4	0.2
Liabilities	0.1	0.1	0.0	0.0
Assets (Capital Expenditure)	9.8	4.7	5.0	3.0
Non- Financial Assets	8.8	4.3	5.0	2.8
Financial Assets	0.9	0.5	0.5	0.2
Change in Balances & Statistical discrepancy	0.0	-0.0	-0.1	-0.1
Fiscal Balance	-7.8	-3.8	-5.0	-1.6
Financing	7.8	3.8	5.0	1.7
Domestic	1.8	0.8	1.0	-0.1
Foreign	6.0	2.9	4.0	1.8

Source: Ministry of Finance