MONETARY POLICY COMMITTEE STATEMENT FOR THE THIRD QUARTER OF 2019

Governor's Presentation to the Media

November 20, 2019

Bank *of* Zambia

OUTLINE OF PRESENTATION

1. Decision of the Monetary Policy Committee
2. Inflation Outturn and Outlook
3. GDP Growth Prospects
4. Monetary Operations
5. Government Securities Market
6. Interest Rates
7. Domestic Credit
8. Money Supply
9. Foreign Exchange Market
10. Global Economic Growth
11. Selected Commodity Prices
12. Current Account
13. Gross International Reserves
14. Conclusion

DECISION OF THE MONETARY POLICY COMMITTEE

- **At its Meeting held on November 18 – 19, 2019, the Monetary Policy Committee decided to raise the Policy Rate by 125 basis points to 11.50%.**

- **In arriving at the decision, the Committee took into account:**

  - **The rise in inflation with projections indicating inflation remaining above the upper bound of the target range over the entire forecast horizon (Q4 2019 - Q3 2021) as upside risks to inflation have heightened and some of them have materialised; and**

  - **The need to restore macroeconomic stability.**

- **The Committee was mindful of the marked deceleration in growth and risks to financial stability.**

INFLATION OUTTURN AND OUTLOOK

Inflationary pressures heightened in the third quarter, reflecting persistent rise in food prices and the pass-through from the depreciation of the Kwacha.

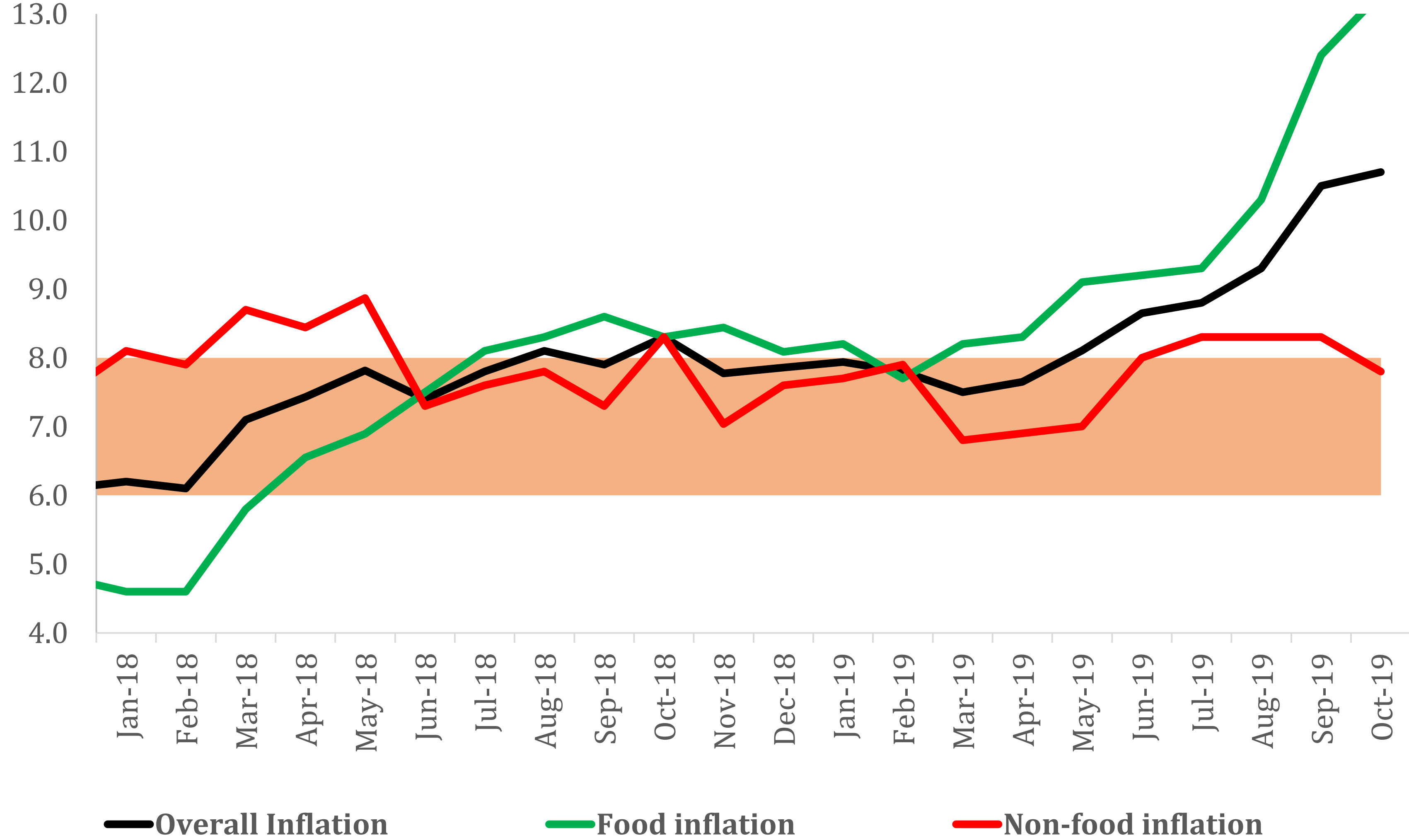
Figure 1: Inflation outcomes (%)

	Q3 2019 Outcome (Quarterly Averages)	Q2 2019 Outcome (Quarterly Averages)	Q3 2019 End-period	Q2 2019 End-period
Overall Inflation	9.5	8.1	10.5	8.6
Food Inflation	10.7	8.9	12.4	9.2
Non-food Inflation	8.3	7.3	8.3	8.0

In October, overall inflation rose to 10.7% as food inflation increased to 13.3% while non-food inflation slowed down to 7.8%.

INFLATION OUTTURN AND OUTLOOK

Figure 2: Inflation Developments, y-o-y (%)



INFLATION OUTTURN AND OUTLOOK

- **On account of heightened upside risks, inflation is projected to remain above the upper bound of the 6-8% target range over the entire forecast horizon (Q4 2019 – Q3 2021).**

- **The risks, which manifest through the expectations and exchange rate channels, include:**

  - **persistent high food prices;**
  - **electricity shortages leading to extended load shedding;**
  - **slower than anticipated progress on fiscal consolidation; and**
  - **high external debt service payments.**

REAL GDP GROWTH

- **Annual real GDP growth for 2018 was revised upwards to 4.0% from 3.7%.**

- **In the second quarter of 2019, real GDP grew by 2.3%, down from 3.9% during the corresponding period in 2018.**

    - **Contraction in mining output, construction as well as transport and storage accounts for the slowdown in real GDP growth.**

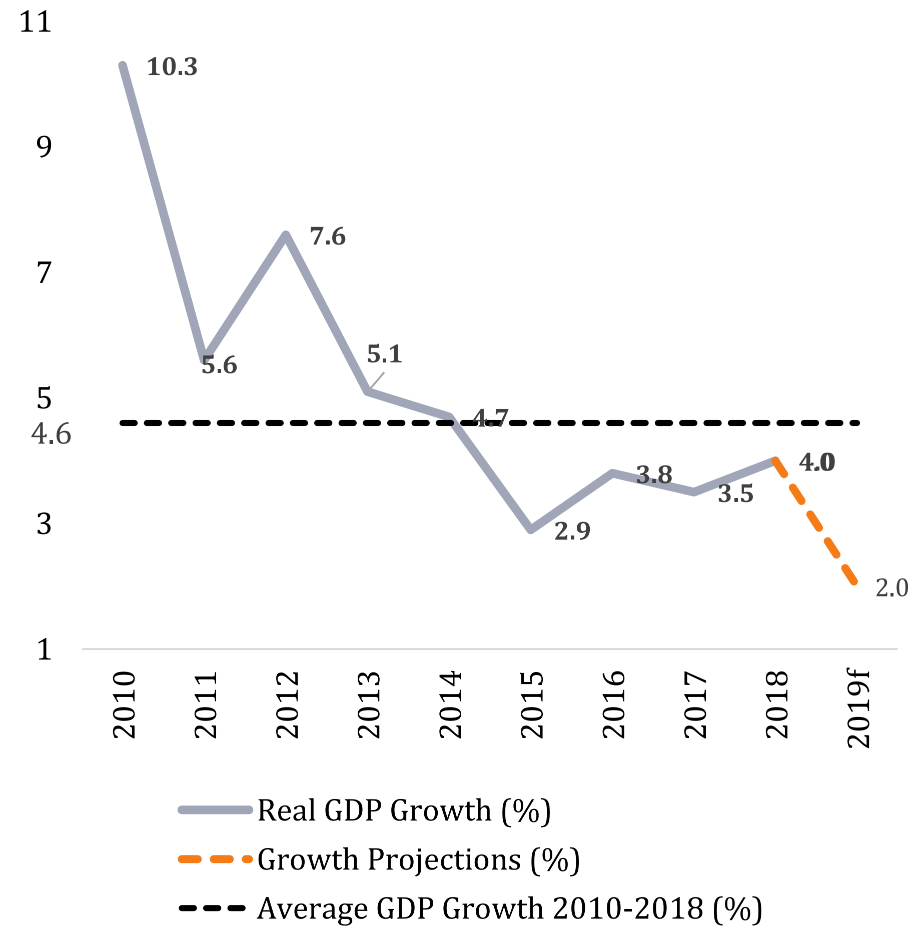
GDP GROWTH PROSPECTS

- **Economic activity is projected to remain subdued and the recovery is weak.**

- **In 2019, GDP is projected to significantly decline to about 2.0% from 4.0% in 2018 premised on projected contraction in agriculture, constrained electricity generation, and lower than anticipated mining output.**

- **This calls for concerted efforts by all economic agents to put back on an upward and strong growth path.**

Figure 3: Annual GDP Growth(Percent)



MONETARY OPERATIONS

- **Money market liquidity conditions remained tight in Q3 due to net Government revenue. Therefore, banks increased their utilisation of the Overnight Lending Facility Window more than in the previous quarter.**

- **However, BoZ foreign exchange purchases injected liquidity and contributed to the rise in the aggregate current account balance to K1.8 billion from K0.9 billion (Figure 5).**

- **The average overnight interbank rate rose to a quarterly average of 10.76% from 10.05% in Q2 on account of tight liquidity conditions (Figure 4).**

MONETARY OPERATIONS

Figure 4: BoZ Policy Rate and Interbank Rate (%)

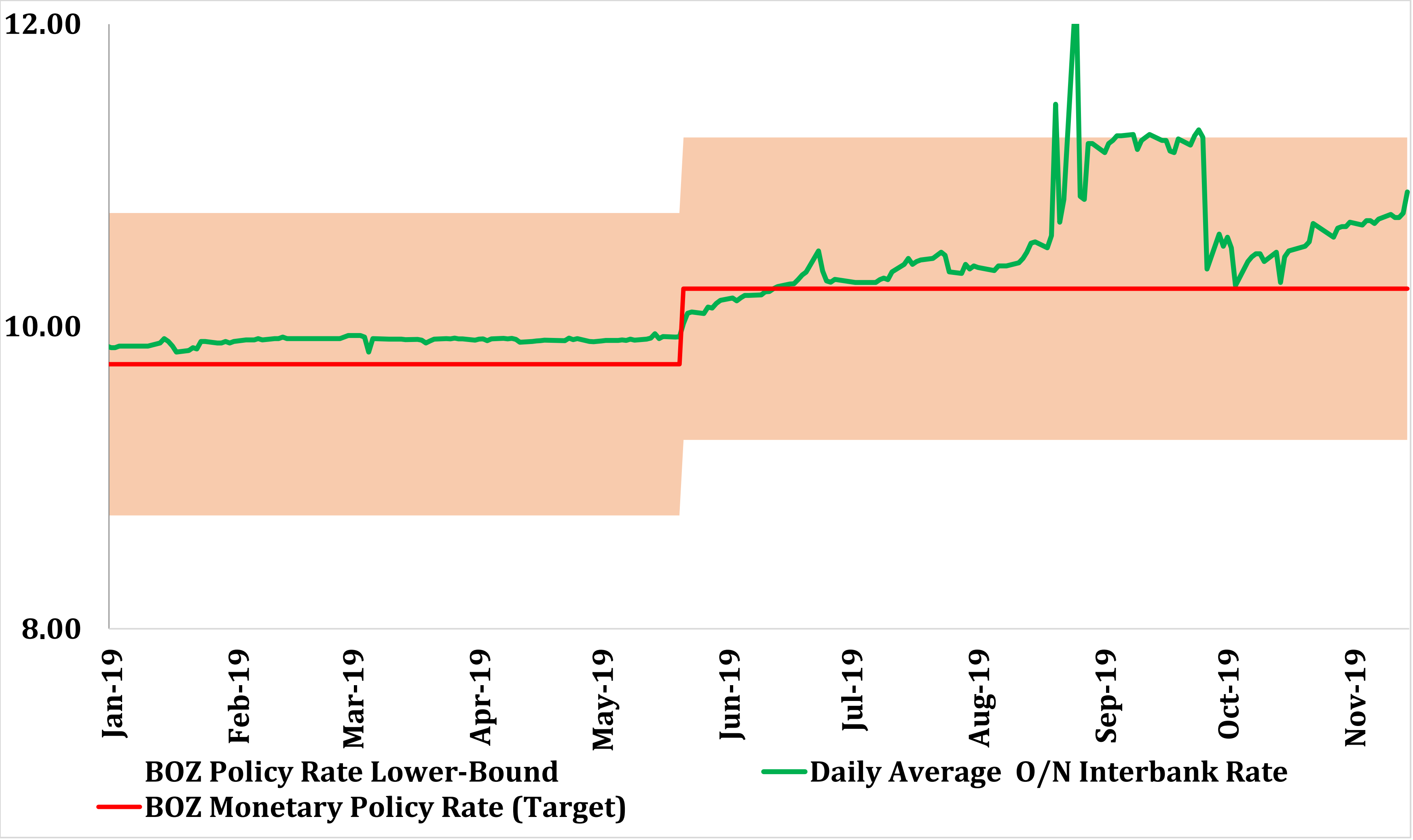


Figure 5: Liquidity Influences (K' bln)

	2018 Q4	2019 Q1	2019 Q2	2019 Q3
Opening balance	**2.5**	**1.4**	**2.2**	**0.9**
Net Govt spending (+)/Revenue (-)	-0.1	-3.8	-4.2	-2.7
BoZ FX influence	0.4	1.3	1.9	4.1
CIC	-0.7	1.0	-1.2	0.0
Change in SR deposits	-1.0	-0.5	0.2	-0.5
OLF	-0.6	-0.1	0.0	0.6
Net Government securities influence	0.4	2.4	0.0	1.0
Open market operations	0.0	0.0	1.5	-1.5
Miscellaneous	0.6	0.2	0.4	0.2
Closing balance	**1.4**	**2.2**	**0.9**	**1.8**

MONETARY OPERATIONS

On 14 November 2019 the Bank of Zambia raised the Overnight Lending Facility (OLF) rate to 28% from 18%.

The increase in the OLF rate was aimed at instilling stability in the market and reining in inflationary pressures.

With the 125 basis points increase in the Policy Rate to 11.50%, the OLF rate will be 16.5 percentage points above the Policy Rate and remains at 28%.

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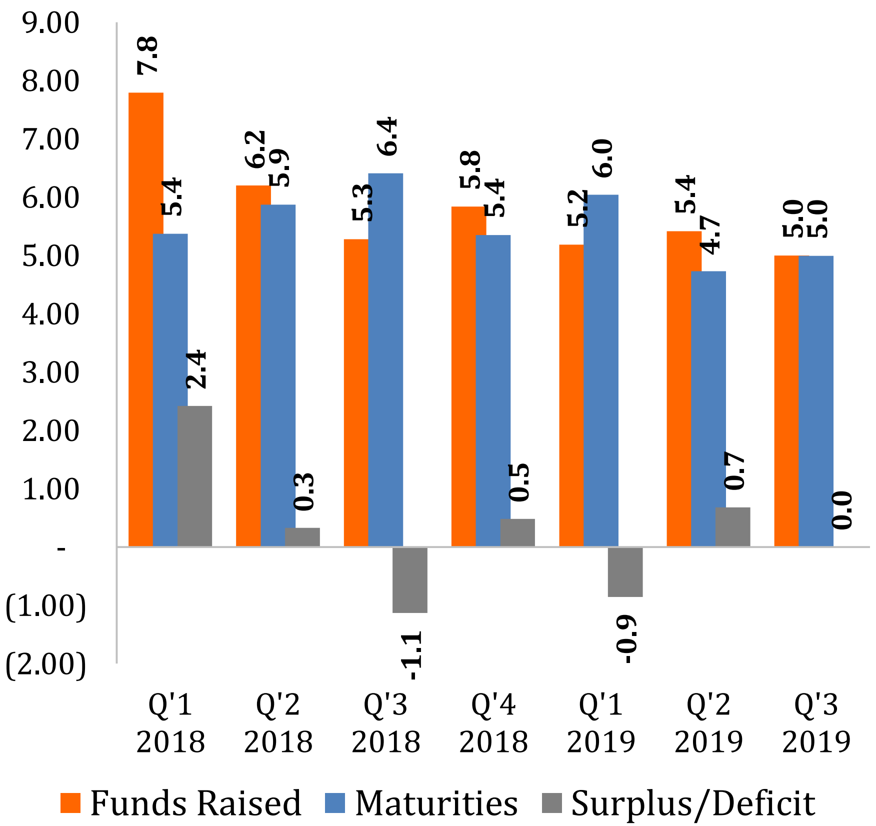
Subscription rates for Government securities remained subdued.

Figure 6: Demand for Govt. Securities (K'bln)

	Amount on offer	Amount Received	Subscription rate (%)
T-bills			
2019Q2	6.7	5.3	79
2019Q3	6.7	5.0	75
Bonds			
2019Q2	3.3	0.5	15
2019Q3	1.7	0.6	35

Figure 7: Funds raised and maturities (K'bln)



GOVERNMENT SECURITIES MARKET

Stock of Government securities rose by 20% to K72.3 billion while non-residents' holdings declined by 9.7% to K7.4 billion

Figure 8: Demand for Treasury bills (K 'mn)

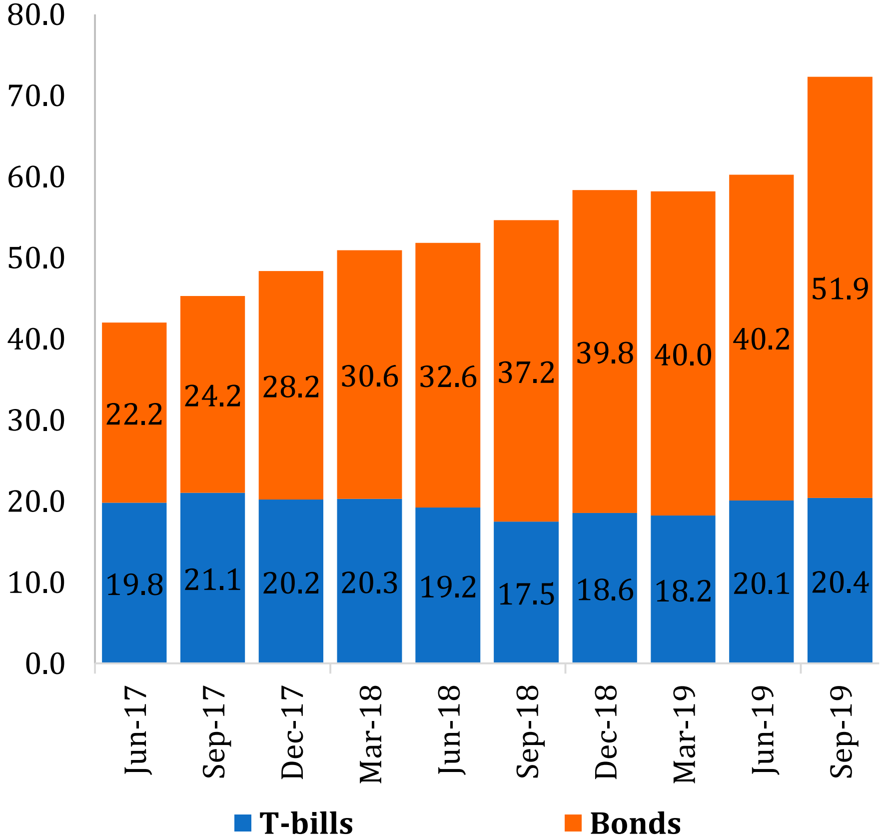
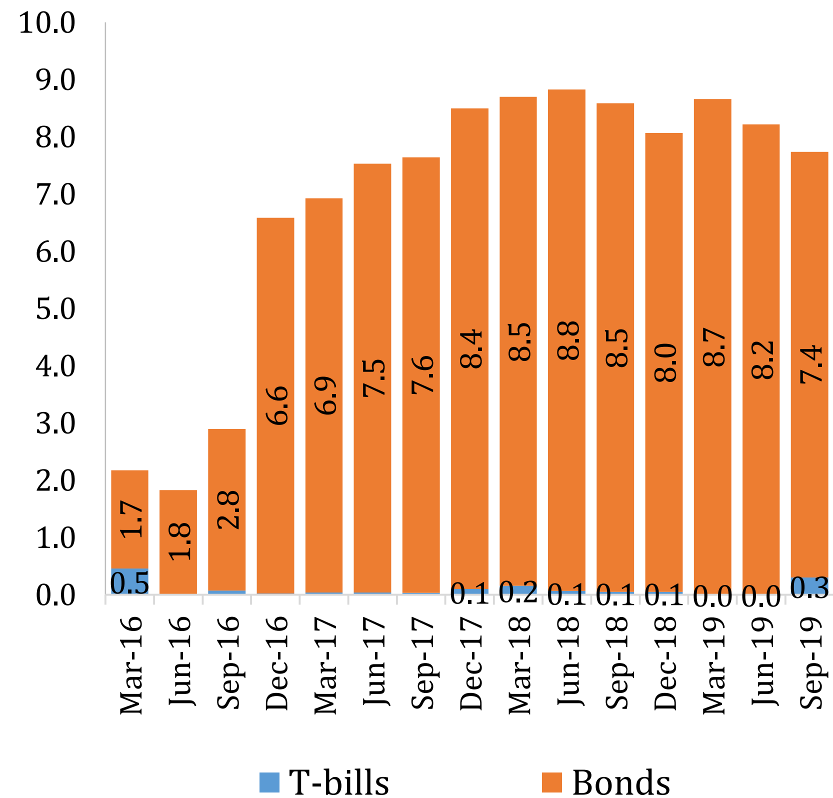


Figure 9: Non-Resident holdings of Government Securities (K'bln)

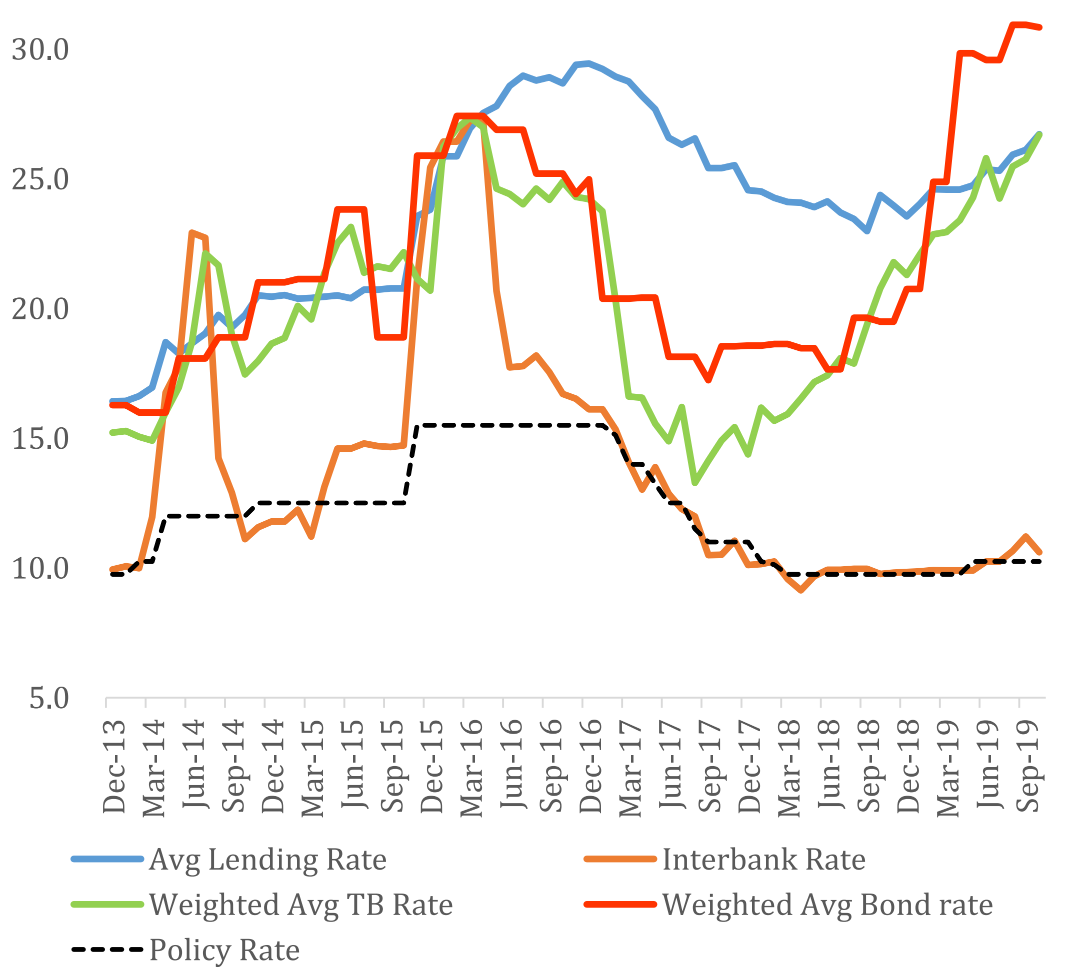


INTEREST RATES

Interest rates continued edging up reflecting the rise in the cost of funds and yield rates on Government securities.

Due to subdued demand, yield rates on Government securities rose further. Treasury bills weighted average rate rose to 25.3% from 24.3% while that for Government bonds rose 30.9% from 29.7%.

Figure 10: Interest Rates (%)



INTEREST RATES

- **The range of interest rates on new Kwacha deposits widened to 1.0% - 26.5% from 2.0% - 24.0% the preceding quarter.**

  The average lending rate (ALR) rose to 26.1% in September 2019 from 25.4% in June (Figure 11).

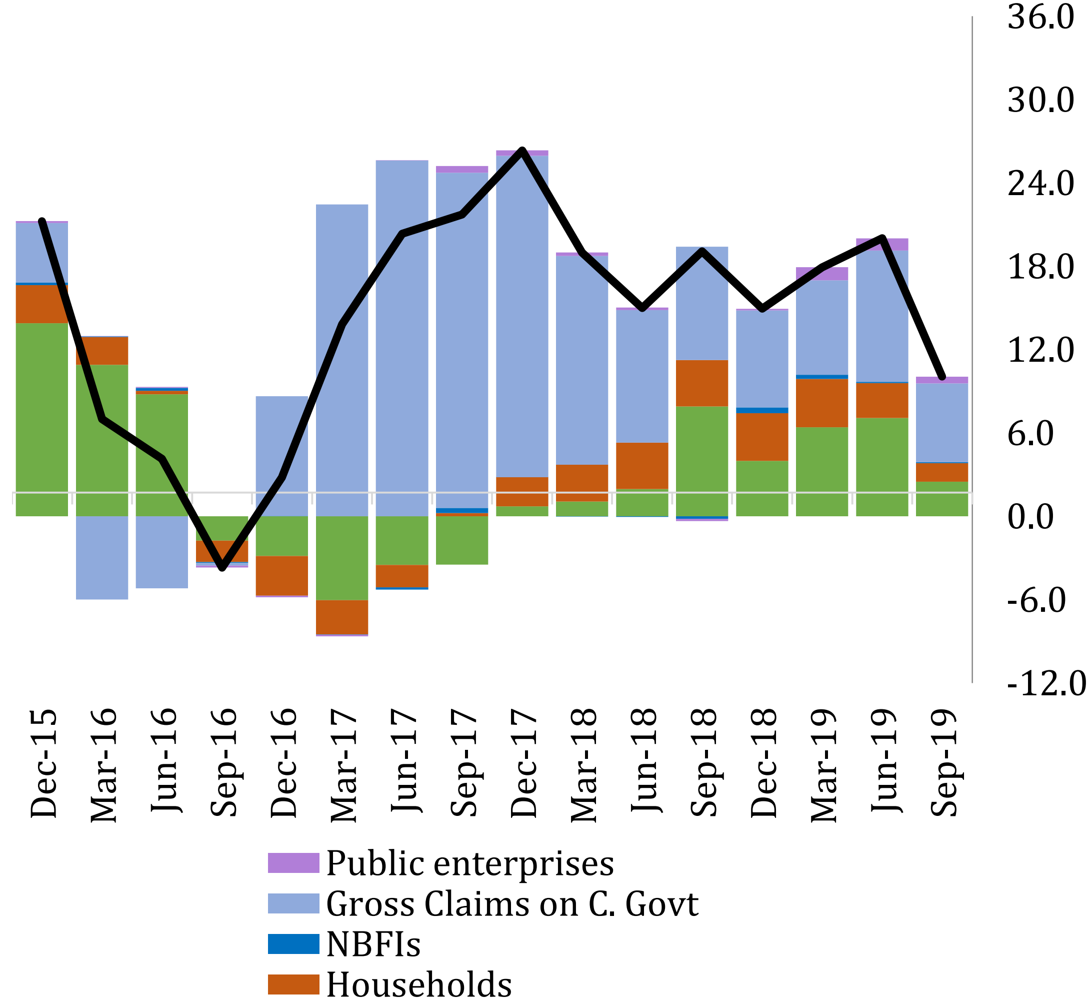
  Excluding outliers, the ALR rose to 23.9% in September from 22.8% in June.

DOMESTIC CREDIT

Domestic credit growth declined to 10.1%, y-o-y, in September 2019 from 20.0% in June 2019 due to lower growth in lending across all sectors.

The reduction in domestic credit growth largely reflects subdued economic activity and tight liquidity conditions.

Figure 11: Contribution to Y/Y Domestic Credit growth

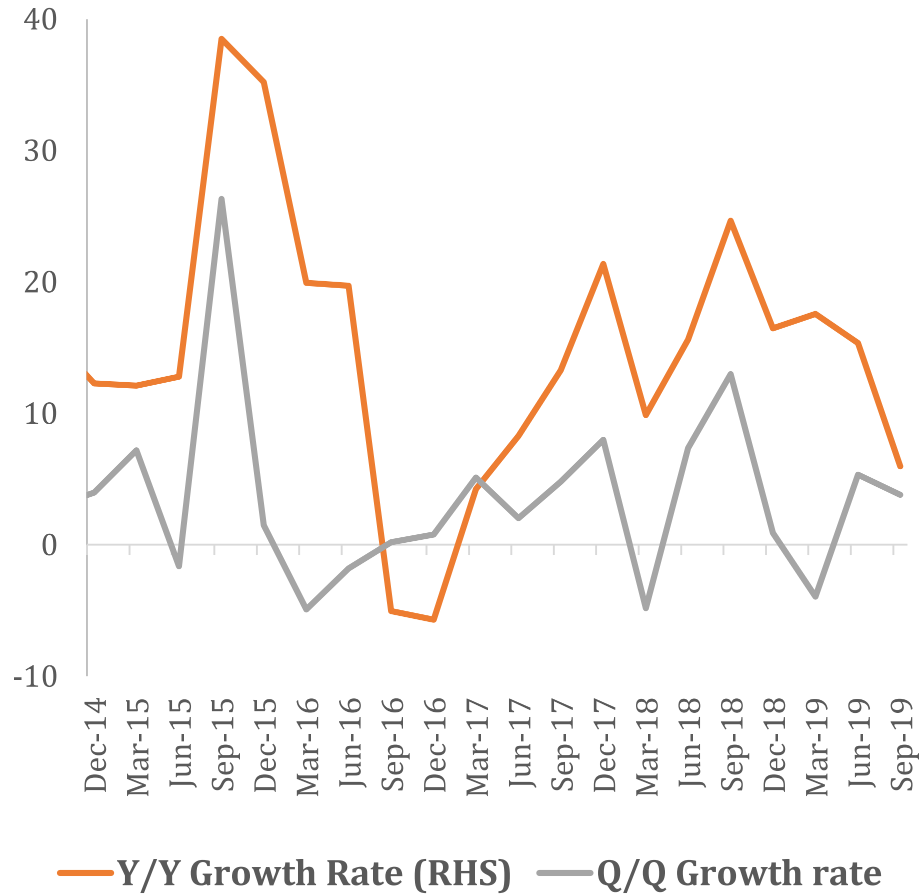


MONEY SUPPLY

Money supply (M3) growth slowed down further to 6.0%, y-o-y, in September 2019 from 15.4% in June 2019.

The slowdown was due to the decline in the growth of credit to both private sector and Government.

Figure 12: Money supply growth (%)



FOREIGN EXCHANGE MARKET

The Kwacha depreciated against the US dollar, but appreciated against other major currencies.

Against the US dollar, the depreciation was mainly on account of high demand for foreign exchange for petroleum imports.

Figure 13: Nominal Exchange Rates

Period	ZMW/USD	ZMW/GBP	ZMW/EUR	ZMW/ZAR
Q2	12.89	16.54	14.47	0.89
Q3	12.97	15.98	14.41	0.88
% chg	0.7	-3.4	-0.4	-1.2

FOREIGN EXCHANGE MARKET

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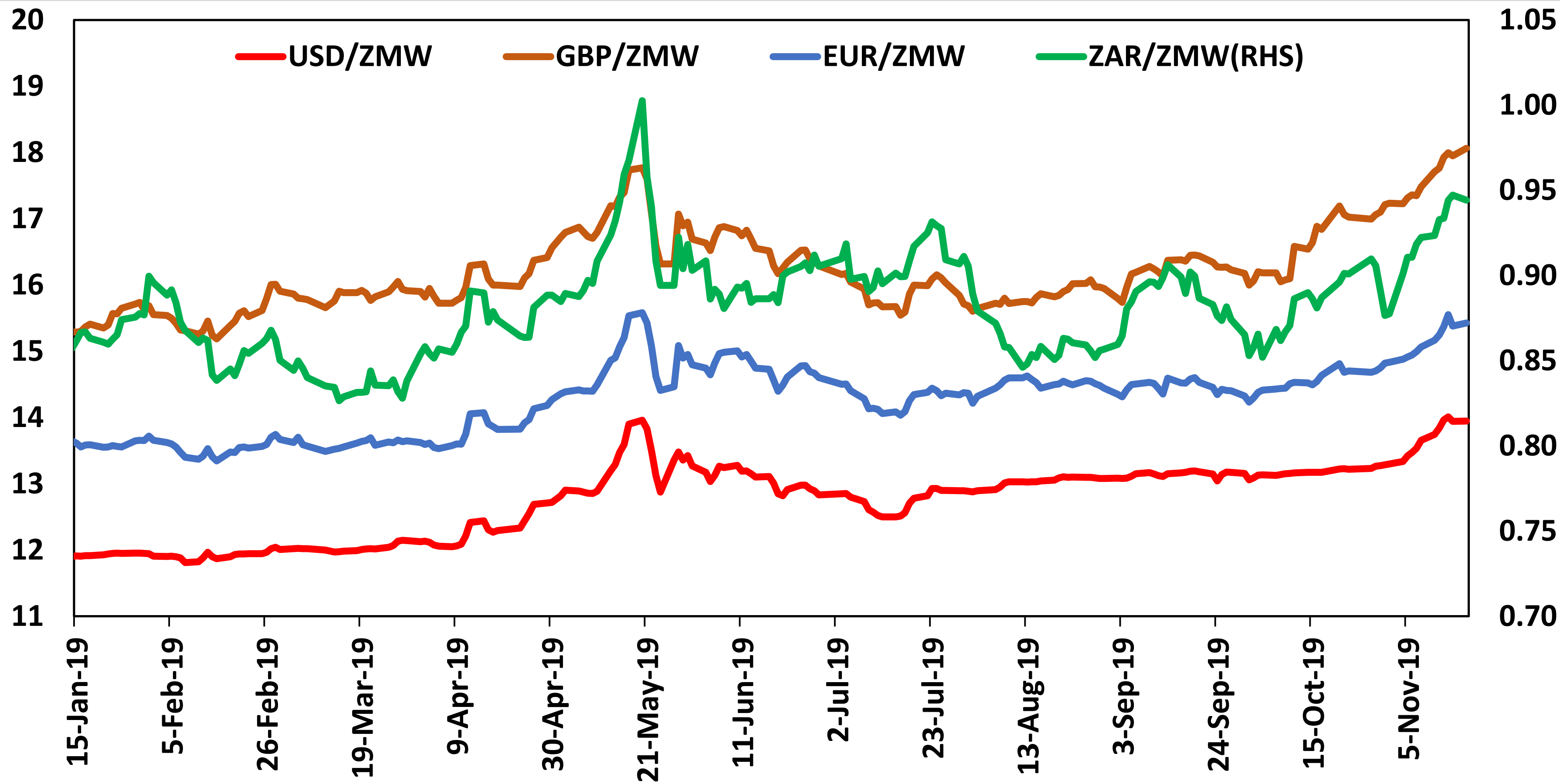
However, beginning November, the Kwacha has come under pressure. As of November 19, 2019, the Kwacha was trading at about K14.00 due to increased demand for petroleum and fertiliser imports as well as adverse market expectations associated with indicated electricity imports to help mitigate the shortfall in domestic supply.

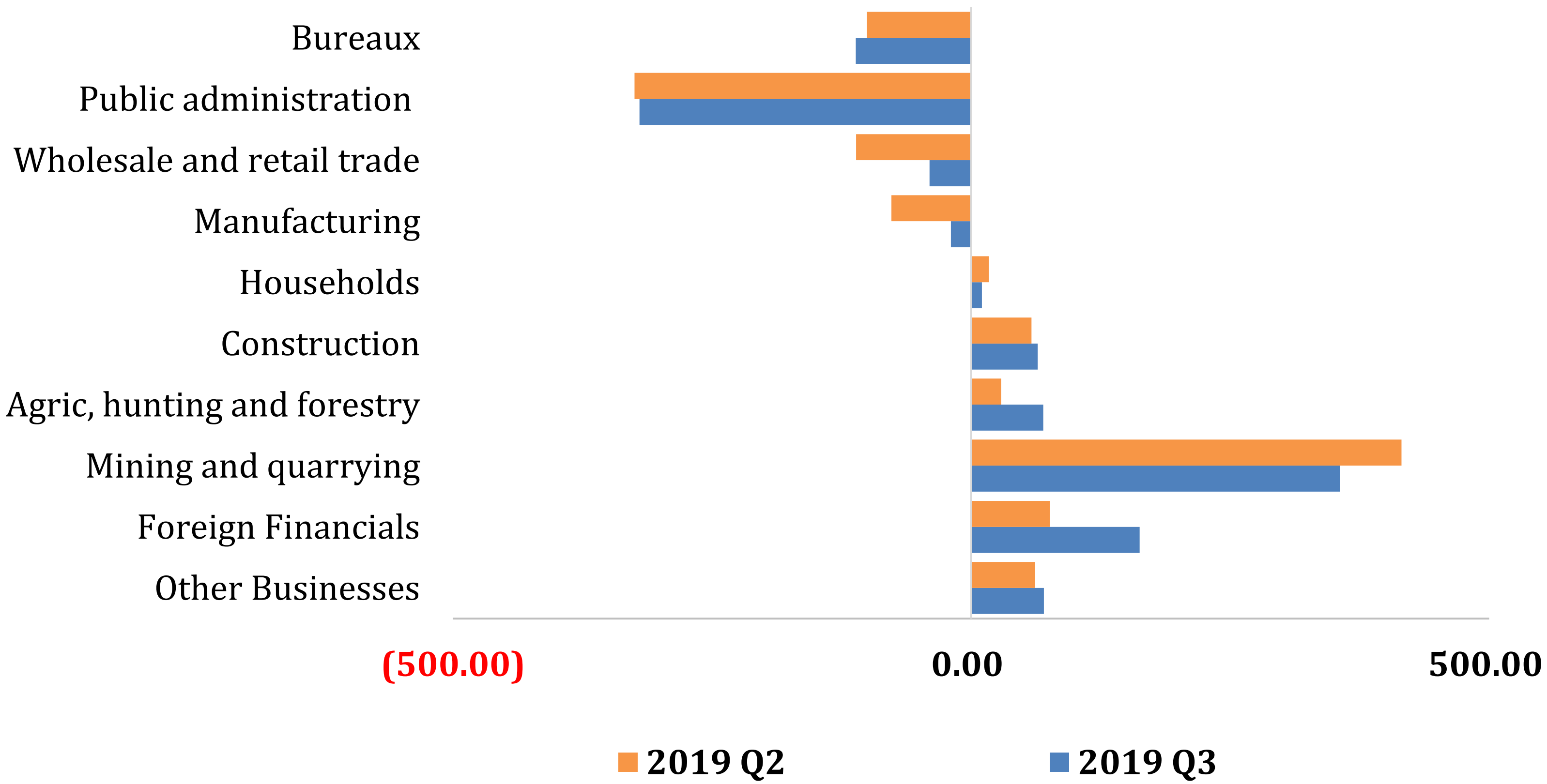
Figure 14: Nominal Exchange Rates



FOREIGN EXCHANGE MARKET

The main suppliers of foreign exchange continued to be the mining sector and foreign financials, but supply declined in the third quarter.

Figure 15: Foreign Exchange Supply and Demand (US$' million)



GLOBAL ECONOMIC GROWTH

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Global growth and growth in Zambia's trading partner countries continue to lose momentum in Q3 2019, reflecting:

- **Persistent trade tensions;**
- **Declining business and consumer confidence;**
- **Heightened policy uncertainty (Brexit) ; and**
- **Geopolitical tensions in the Middle East**

In October 2019, global growth was further revised downwards to 3.0% and 3.4% in 2019 and 2020 from the July forecasts of 3.2% and 3.5%, respectively (IMF WEO, October 2019).

SELECTED COMMODITY PRICES

In Q3 2019, copper and crude oil prices declined by 3.4% and 7.9%, respectively. This reflects mainly slowing global growth.

Figure 16: Commodity Prices

	2018 Q3	2018 Q4	2019 Q1	2019 Q2	2019 Q3
Copper Price (US$/ton)	6,118.0	6,164.0	6,226.0	**5,947.1**	**5,742.0**
Oil Price (Dubai) (US$/barrel)	74.0	66.8	63.3	**64.5**	**59.4**
Wheat (US$/ton)	208.8	221.6	212.6	**206.7**	**204.1**
Maize Price (US$/ton)	157.9	162.8	167.5	**175.9**	**162.7**
Cotton (US$/kg)	2.1	1.91	1.82	**1.80**	**1.59**
Sugar (US$/kg)	0.3	0.3	0.3	**0.3**	**0.3**
Soya beans (US$/ton)	370.0	374.0	378.0	**353.0**	**369.6**

CURRENT ACCOUNT

Preliminary data for Q3 2019 indicate a current account deficit of US$92.4 million (1.6% of GDP) compared to a surplus of US$80.7 million (1.4% of GDP) in Q2 2019. The turnaround in the current account balance was mainly due to a reduction in the balance on goods surplus.

Table 17: Balance of Payments (US$' million)

	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019
Current Account Balance	**131.6**	**112.2**	**55.6**	**80.7**	**-92.4**
Balance on Goods	**194.6**	**-98.7**	**348.3**	**281.7**	**92.4**
Total Exports	**2,289.7**	**2,094.6**	**1,986.8**	**1,960.9**	**1,707.4**
Copper	1,628.6	1,480.9	1,431.9	1,320.3	1,013.7
Cobalt	28.7	17.5	3.3	0.0	0.0
Gold	31.3	36.9	43.2	46.0	50.1
NTEs	583.5	541.7	489.7	575.8	624.8
Total Imports	**2,095.1**	**2,193.3**	**1,638.5**	**1,679.2**	**1,612.3**
Primary Income	**30.9**	**309.3**	**-225.2**	**-131.8**	**-151.1**
Secondary Income	68.9	70.2	79.2	83.7	85.0
Services Account	-162.8	-168.7	-146.8	-153.0	-118.6
Capital Account	16.3	16.3	17.9	39.9	19.5
Financial Account	355.0	147.0	225.7	47.8	-130.4
Net Errors/Omissions	37.7	-25.0	-13.2	-15.2	18.1
Overall Balance	**169.4**	**43.5**	**161.3**	**-58.7**	**-75.6**
Change in Reserve Assets	-172.0	-72.0	-163.9	31.8	73.1

GROSS INTERNATIONAL RESERVES

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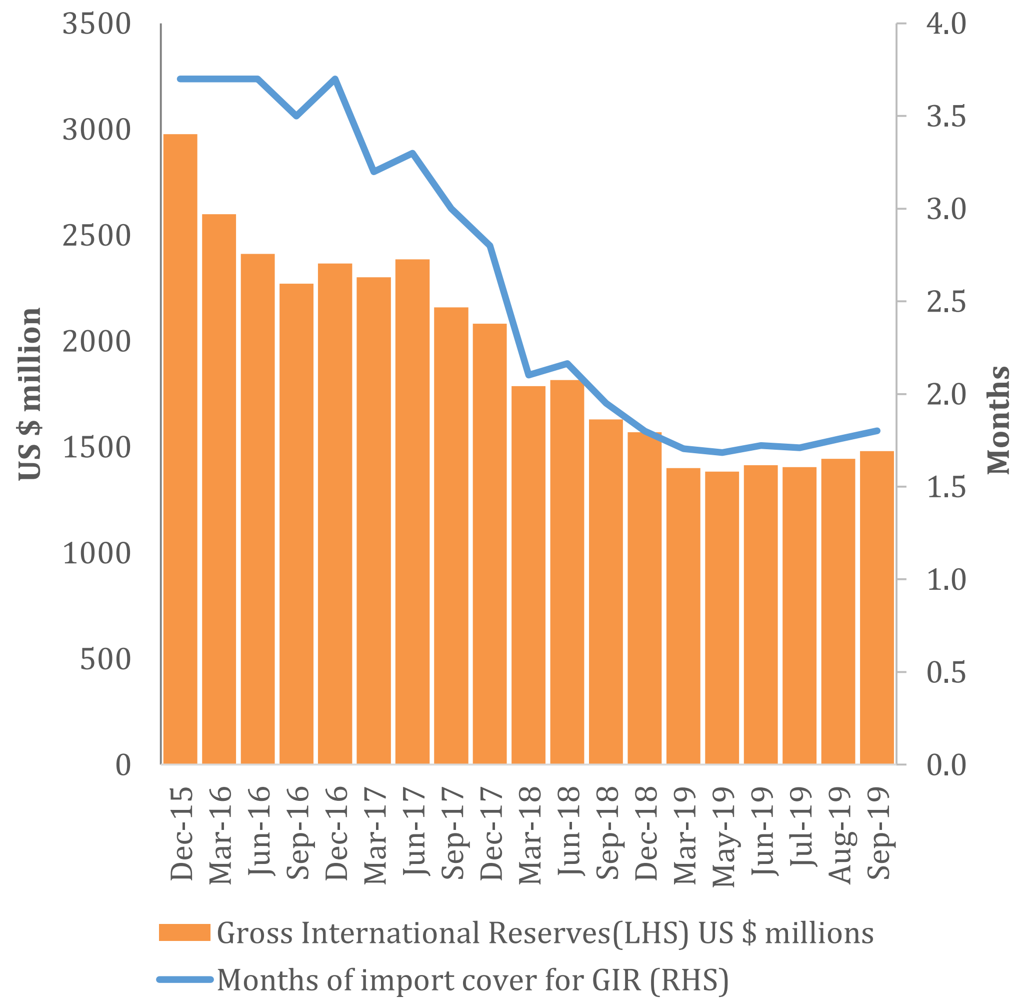
Despite high external debt service payments, gross international reserves (GIR) rose to US$1.5 billion at end-September 2019 (equivalent to 1.8 months of import cover), from US $1.4 billion (equivalent to 1.7 months of import cover) in June 2019.

BoZ net foreign exchange purchases and mineral royalty tax receipts amounting to US$281.1 million and US$51.5 million, respectively accounted for the increase in GIR.

Figure 18: Gross International Reserves



CONCLUSION

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The MPC noted rising inflationary pressures in Q3, with projected inflation remaining above the upper bound of the 6-8% target range over the entire forecast horizon (Q4 2019 – Q3 2021).

This necessitated the hike in the Policy Rate to bring inflation back into the target range over the medium-term.

The MPC was mindful of the marked deceleration in growth and risks to financial stability. In this regard, the MPC recognised the importance and need for other tools that include macro prudential and fiscal policy measures to address these risks.

Furthermore, and as indicated in previous MPC Statements, monetary policy alone is not sufficient to address prevailing economic challenges and to restore macroeconomic stability. It must be complemented by corrective fiscal and structural policy measures

THANK YOU
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