# MONETARY POLICY COMMITTEE STATEMENT FOR THE SECOND QUARTER OF 2020

## Governor's Presentation to the Media

August 19, 2020

Bank *of* Zambia

# OUTLINE OF PRESENTATION

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

# DECISION OF THE MONETARY POLICY COMMITTEE

**At its Meeting held on August 17–18, 2020, the Monetary Policy Committee decided to reduce the Policy Rate by a further 125 basis points to 8.0%.**

**Key factors the Committee took into account in arriving at its decision were:**

- **the need to safeguard financial stability, people's lives and livelihoods in the wake of the COVID-19 pandemic;**
- **the projected steady decline in inflation towards the upper bound of the medium-term target range at the end of the forecast period; and**
- **significant worsening in economic conditions over the second quarter, and much weaker growth prospects in 2020 than earlier anticipated.**

# GLOBAL ECONOMIC GROWTH

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**Global growth is projected to contract significantly by 4.9% in 2020, a downward revision from 3.0% earlier projected (IMF WEO, June 2020 Update). This largely reflects a deeper and more protracted negative impact of the COVID-19 pandemic.**

**Measures taken to contain the pandemic are severely constraining private consumption, investment, trade, and travel, resulting in weakening global demand.**

**Consequently, output and employment have fallen, as manufacturing activity has declined sharply due to supply chain disruptions and factory shutdowns.**

**The services sector, particularly transport and tourism sub-sectors, have continued to be the most adversely affected.**

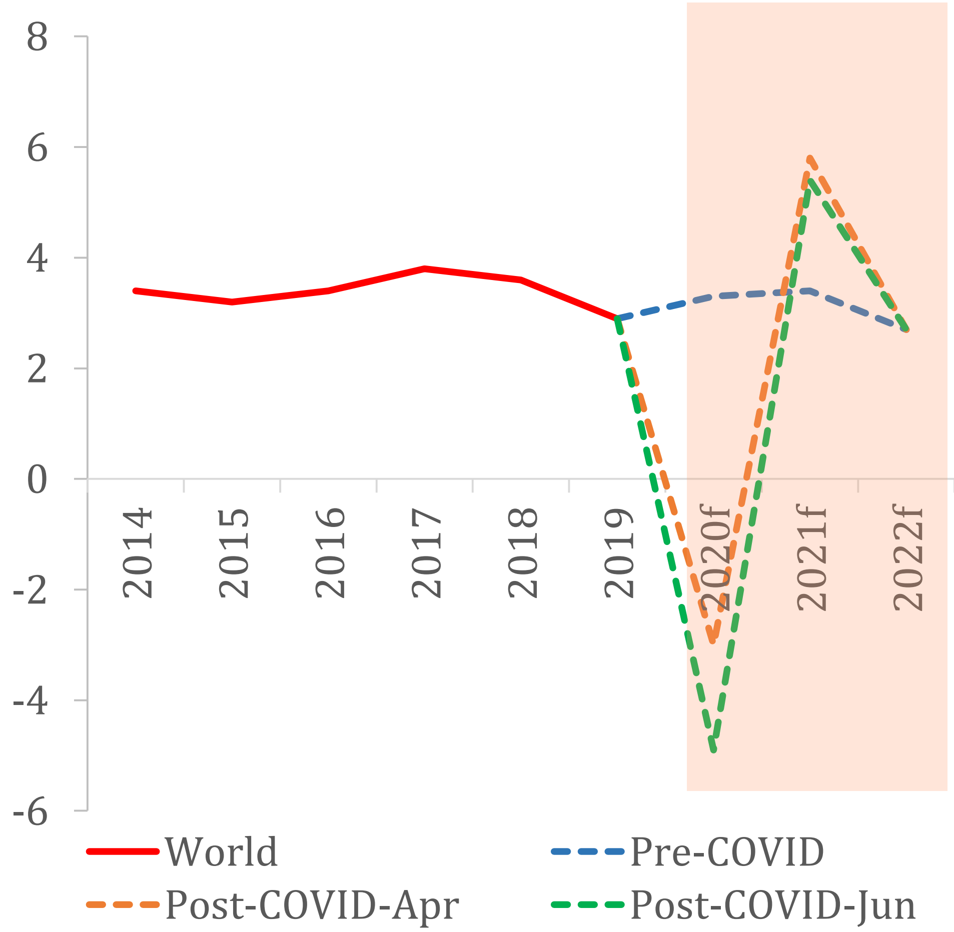
# GLOBAL ECONOMIC GROWTH

**In 2021, global growth is projected to recover to 5.4% against an earlier projection of 5.8%.**

**Policy measures taken by governments and central banks around the world are expected to support the recovery.**

**However, there is a high degree of uncertainty surrounding the forecast as recovery will depend on the evolution of the pandemic as well as the speed of developing and delivering a vaccine and treatment.**

**Figure 1: Pre and With-COVID-19 Global GDP Growth Projections (annual, percent)**




**Source: IMF World Economic Outlook for January and April 2020 Update, Focus Economics**

## DOMESTIC ECONOMIC ACTIVITY AND OUTLOOK

**As at August 18, 2020, COVID-19 cases in Zambia had risen to 9,981 from 832 at the time of the May MPC Meeting.**

**The rapid rise in cases reflects the severity of the pandemic, with a telling effect on domestic economic activity. This has worsened in the second quarter as reflected in company shutdowns, job and income losses, declining business output, and weakening consumer demand.**

**Further, electricity load shedding, and rising production costs, associated with high energy tariffs, have continued to weigh on growth.**

**Results from the *Second Quarter 2020 Bank of Zambia Quarterly Survey of Business Opinion and Expectations* indicate worsening economic conditions with all monitored indicators showing deterioration, except for new orders, largely due to increased demand for pharmaceutical products used to fight COVID-19.**

# DOMESTIC ECONOMIC ACTIVITY AND OUTLOOK

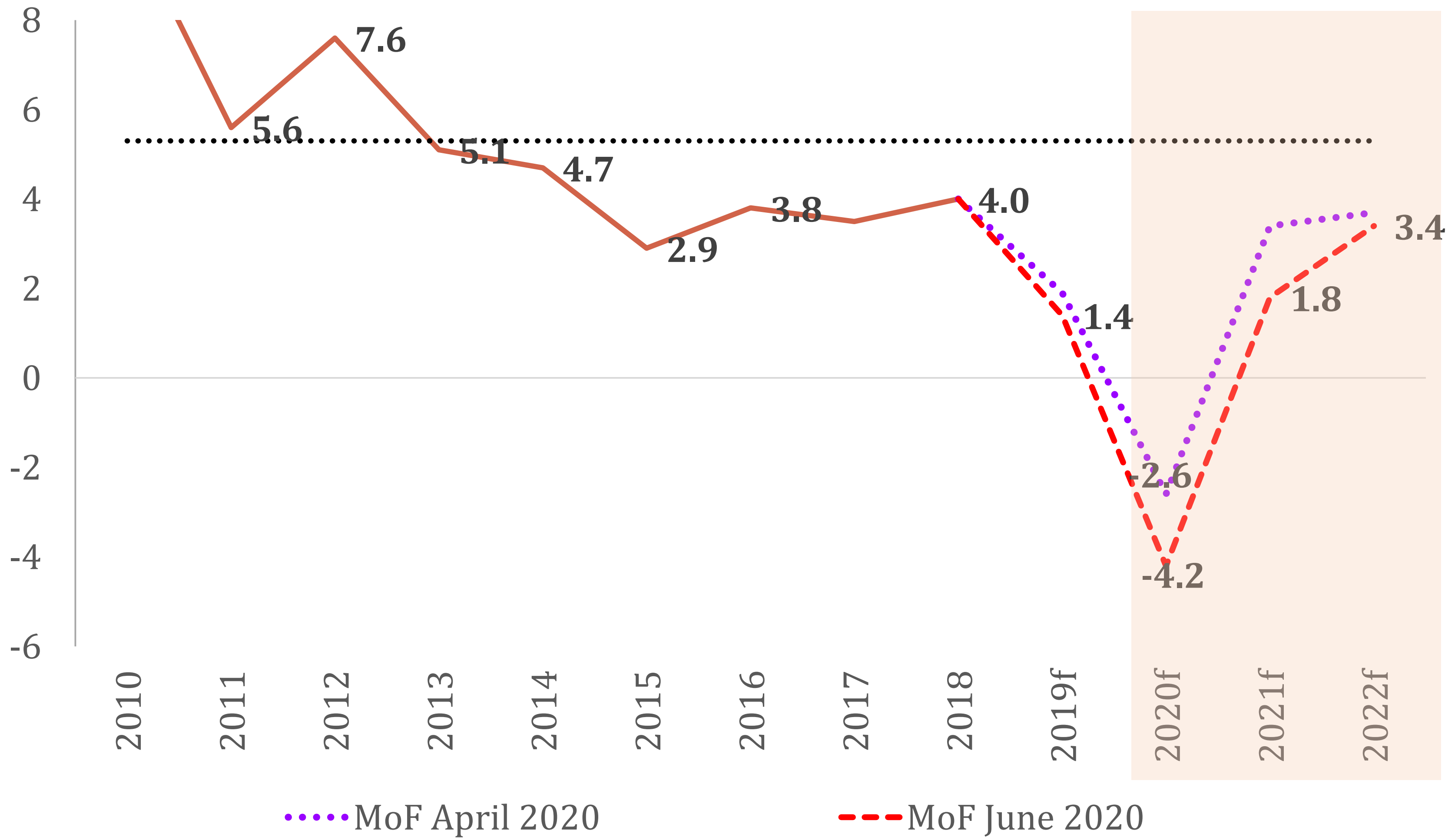
**The *Stanbic Bank Zambia Purchasing Managers Index* also indicates significant deterioration in business conditions for the private sector amid company shutdowns, decline in business output and weak demand.**

**The Zambian economy is projected to contract by 4.2% in 2020, deeper than the earlier projection of 2.6%. This is against a revised preliminary outturn of 1.4% in 2019 (Figure 2).**

**The substantial decline in consumer and investment spending due to disruptions in business operations are expected to continue to constrain economic growth. The most adversely affected sectors are wholesale and retail trade, construction, and tourism.**

# DOMESTIC ECONOMIC ACTIVITY AND OUTLOOK

Figure 2: Annual Real GDP – Actual and Forecast (%), 2010-2022




Source: Ministry of Finance

# INFLATION OUTTURN AND OUTLOOK

**Annual overall inflation continued on an upward trend, rising to an average of 16.1% from 13.5% in the previous quarter (Figures 3 and 4).**

**This was mainly on account of the pass-through from the depreciation of the Kwacha against the US dollar.**

**Figure 3: Inflation outcomes (%)**

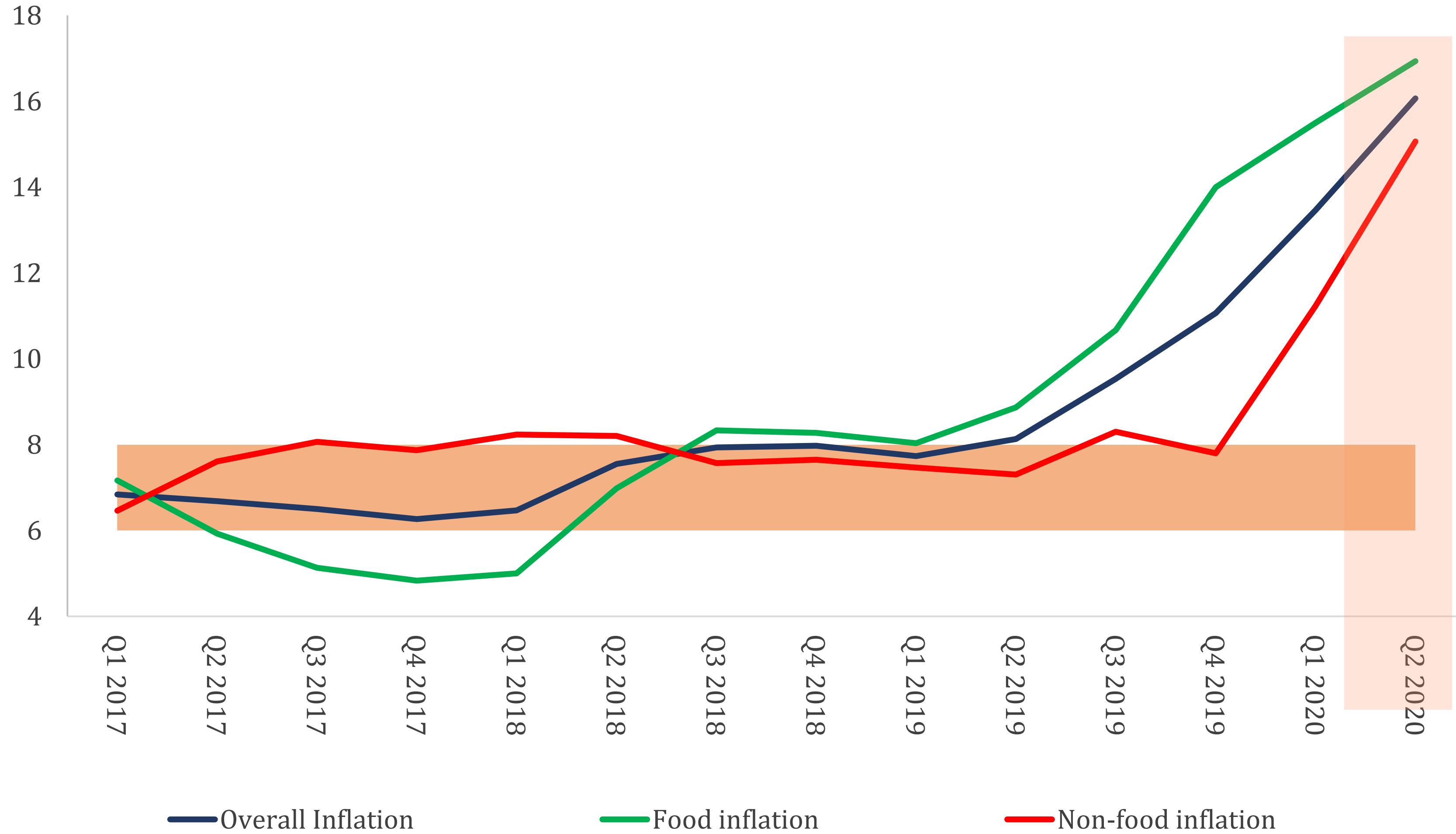
| | Q2 2020 Average | Q1 2020 Average | Q2 2020 End-period | Q1 2020 End-period |
|---|---|---|---|---|
| **Overall Inflation** | **16.1** | **13.5** | 15.9 | 15.7 |
| **Food Inflation** | **16.9** | **15.5** | 16.3 | 15.2 |
| **Non-food Inflation** | **15.1** | **11.2** | 15.5 | 12.7 |

Source: Zambia Statistics Agency

**In July, however, inflation marginally went down to 15.8% from 15.9% in June. This was mainly attributed to the reduction in prices of maize and related products as well as those for seasonal vegetables.**

# INFLATION OUTTURN AND OUTLOOK

## Figure 4: Inflation Developments, y-o-y (%)




Source: Zambia Statistics Agency (ZSA)

# INFLATION OUTTURN AND OUTLOOK

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- **Although projected to remain above the upper bound of the 6-8% medium-term target range, inflation is expected to steadily decline, reaching the upper bound by the end of the forecast horizon.**

- **Expected moderation in food prices due to the significant improvement in the supply of food items, particularly maize is assumed to be the major driver.**

- **Factors keeping inflation above the upper bound of the target range in the earlier part of the forecast horizon, include higher fiscal deficits and the weakening of the global economy.**

- **Risks to the inflation outlook include further deterioration in the fiscal deficit, adverse impact of monetary expansion, a deeper than projected global recession as well as prolonged and extended electricity load shedding.**

- **These risks are likely to exert pressure on inflation through the interest rate, expectations, and/or the exchange rate channels.**

# MONETARY OPERATIONS

- **The overnight interbank rate declined to a quarterly average of 10.98% in the second quarter from 12.56% in the first quarter.**

- **This followed the reduction in the Policy Rate to 9.25% in May 2020 and improvement in liquidity conditions.**

- **Market liquidity increased largely on account of the broader set of measures instituted by the Bank to mitigate the adverse impact of the COVID-19 pandemic on the economy and the financial sector.**

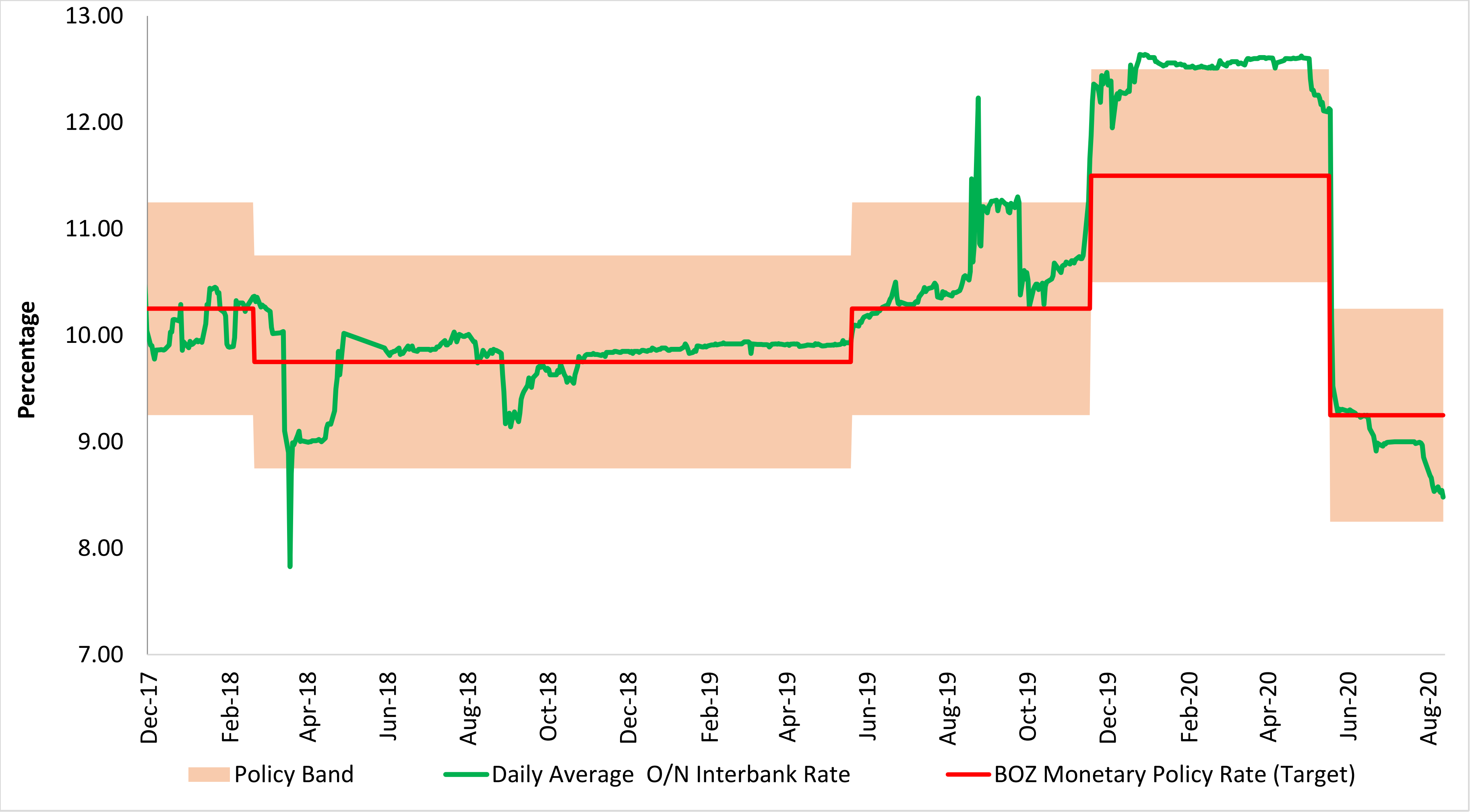
- **The overnight interbank rate was, however, broadly contained within the bounds of the Policy Rate Corridor of 8.25% to 10.25% throughout the quarter (Figure 5).**

# MEASURE TAKEN BY THE BANK OF ZAMBIA

- **Scaling up of open market operations;**
- **Introduction of the Secondary Market Bond Purchase Programme;**
- **Establishment of a K10 billion Targeted Medium-Term Refinancing Facility;**
- **Revision of rules governing the operations of the interbank foreign exchange market;**
- **Revision of loan classification and provisioning rules;**
- **Extension of the requirement of mining companies to pay all their statutory obligations in US dollars;**
- **Initiation of arrangements to engage domestic and non-resident financial institutions in foreign exchange swaps;**
- **Stepped up the sensitization on the use of digital channels and contactless mobile payment mechanisms; and**
- **Implemented Business Continuity protocols.**

# MONETARY OPERATIONS

## Figure 5: Interbank Rate and BoZ Policy Rate (%)




Source: Bank of Zambia

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**The banks' aggregate current account balance rose to K3.0 billion from K1.2 billion, largely on account of net open market operations injections, net Government spending, and BoZ foreign exchange purchases.**

**Figure 6: Liquidity Influences (K' billion)**

| | Q3 2019 | Q4 2019 | Q1 2020 | Q2 2020 |
|---|---|---|---|---|
| Opening balance | 0.9 | 1.8 | 2.0 | 1.2 |
| Net Govt. spending | -2.7 | -1.1 | -2.3 | 1.1 |
| BoZ FX influence | 4.1 | 0.1 | 1.6 | 0.9 |
| Currency in Circulation | 0.0* | -0.3 | 0.4 | -2.1 |
| Change in SR deposits | -0.5 | -1.0 | 0.0 | -1.2 |
| Overnight Lending Facility | 0.6 | 0.1 | -0.3 | 0.5 |
| Net Government securities influence | 1.0 | 2.4 | -0.4 | -0.5 |
| Open market operations | -1.5** | 0.0 | 0.2 | 2.6 |
| Miscellaneous | 0.2 | 0.0 | 0.3 | 0.4 |
| Closing balance | 1.8 | 2.0 | 1.2 | 3.0 |

Source: Bank of Zambia

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**Demand for Government securities improved, reflecting increased liquidity in the market (Figure 7).**

**Funds raised from the auctions significantly increased leading to a surplus of K3.9 billion.**

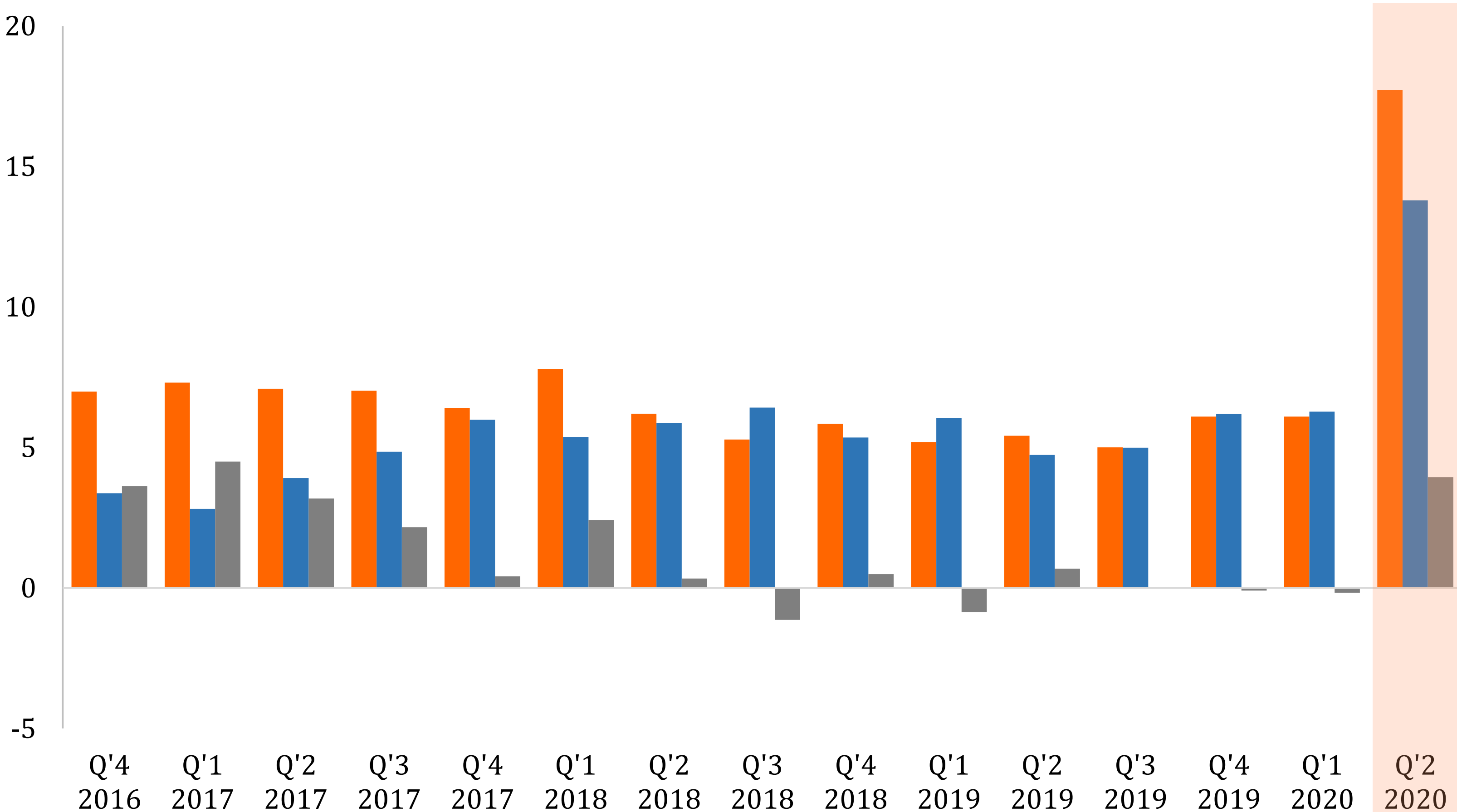
**Figure 7: Demand for Govt. Securities (K' billion)**

| | Amount on Offer | Amount Received | Subscription Rate (%) |
|---|---|---|---|
| **T-bills** | | | |
| 2020Q1 | 6.7 | 5.6 | 84 |
| 2020Q2 | 5.7 | 9.6 | 168 |
| **Bonds** | | | |
| 2020Q1 | 3.3 | 0.9 | 27 |
| 2020Q2 | 3.3 | 1.3 | 39 |

Source: Bank of Zambia

# GOVERNMENT SECURITIES

**Figure 8: Govt. Securities – Funds raised Vs Maturities (K' billion)**



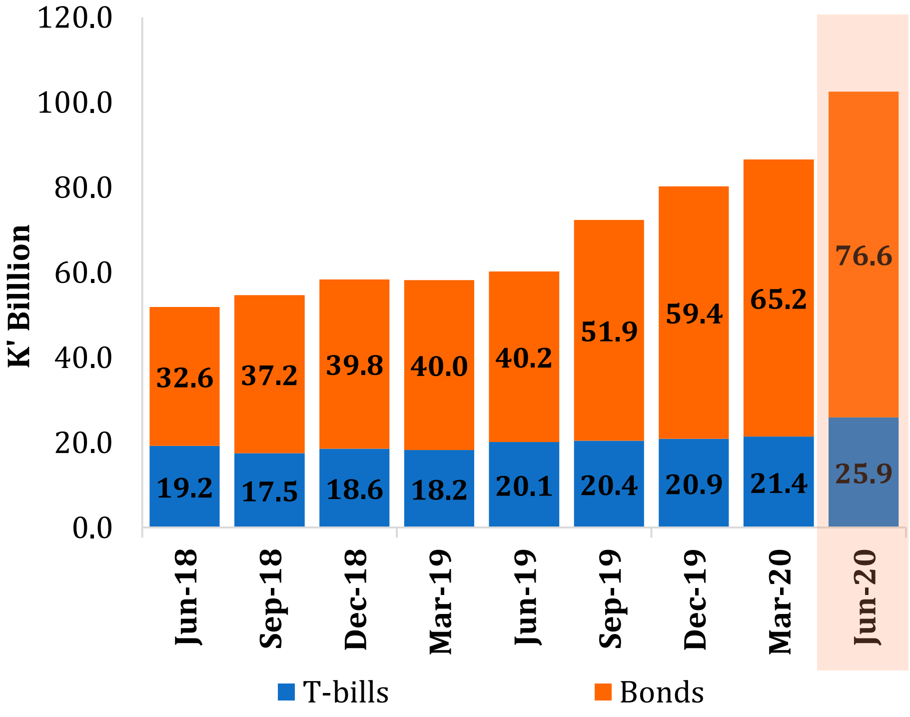

Source: Bank of Zambia

# GOVERNMENT SECURITIES MARKET

**The outstanding stock of Government securities increased by 18.4% to K102.5 billion at end-June as Government's financing needs remain high.**

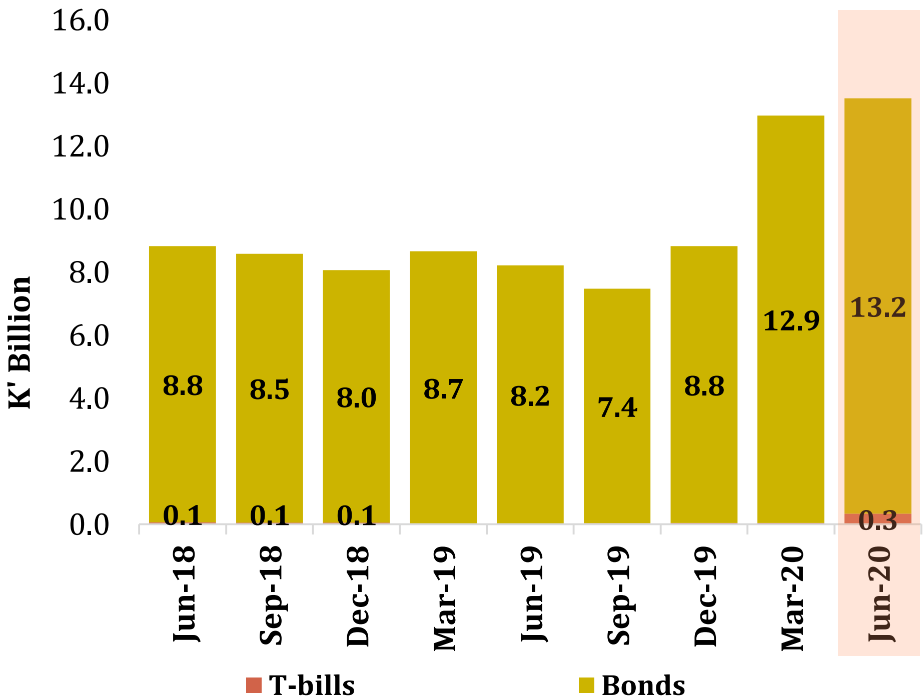
**Holdings by non-residents rose by 4.2% to K13.2 billion, representing 13.2% of the total securities. Virtually all these holdings (97.4%) are in Government bonds.**

**Figure 9: Stock of Govt Securities**




Source: Bank of Zambia

**Figure 10: Non-resident Holdings of Government Securities**




Source: Bank of Zambia

# INTEREST RATES

**Interest rates generally declined, mainly driven by improvements in liquidity conditions and the lowering of the Policy Rate.**

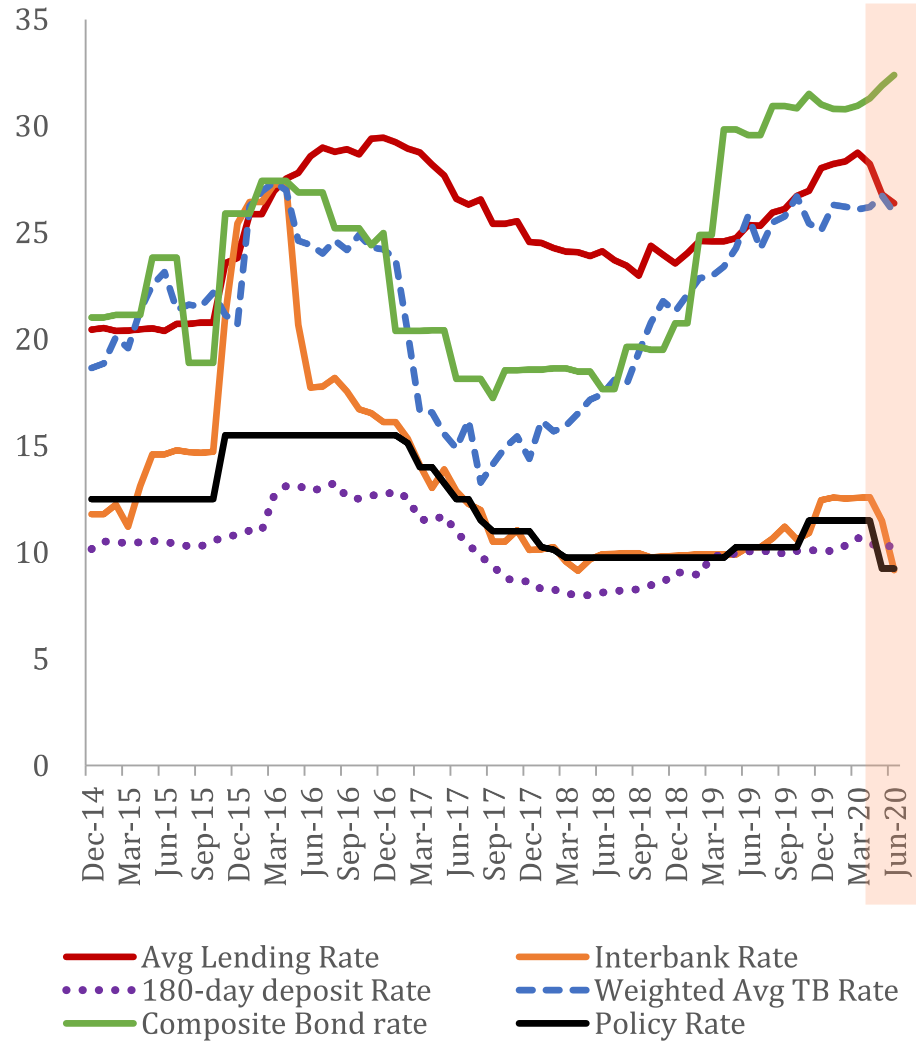
**Commercial banks' nominal average lending rate declined to 26.4% from 28.8%.**

**The savings rate for 180-day deposits declined marginally to 10.3% from 10.7%.**

**The composite Treasury bill yield rate declined slightly to 25.9% from 26.1%.**

**However, the Government bonds composite yield rate rose to 32.4% from 30.9%, largely reflecting investors' high risk premium on long-term investments.**

**Figure 11: Nominal Interest Rates (%)**




Source: Bank of Zambia

# DOMESTIC CREDIT

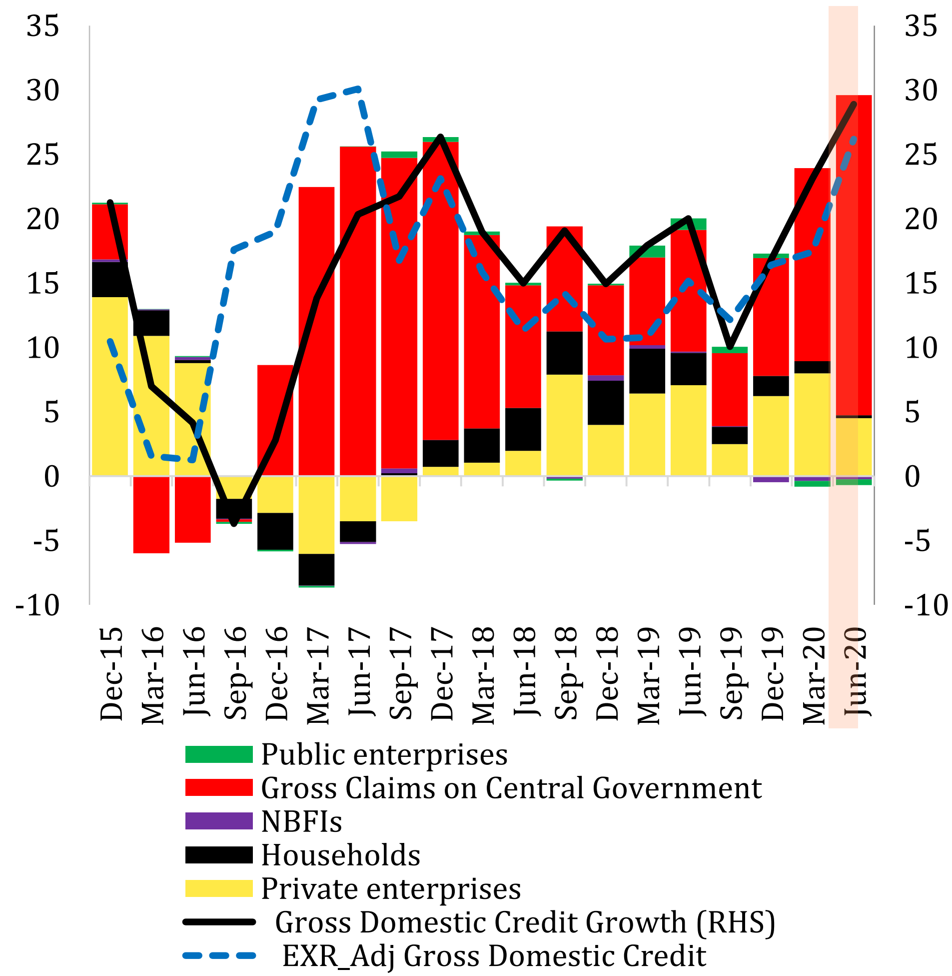
**Growth in credit to the private sector slowed down in the second quarter to 10.4%, y-o-y, from 19.5%.**

**This was on the back of depressed aggregate demand and reduced appetite by banks to lend in the light of heightened default risk due to weakened economic activity.**

**However, credit to Government expanded by 46.9%, y-o-y, compared to 28.6% in March.**

**Government continued to account for a larger proportion of growth in credit.**

**Figure 12: Contribution to Y/Y Domestic Credit growth**



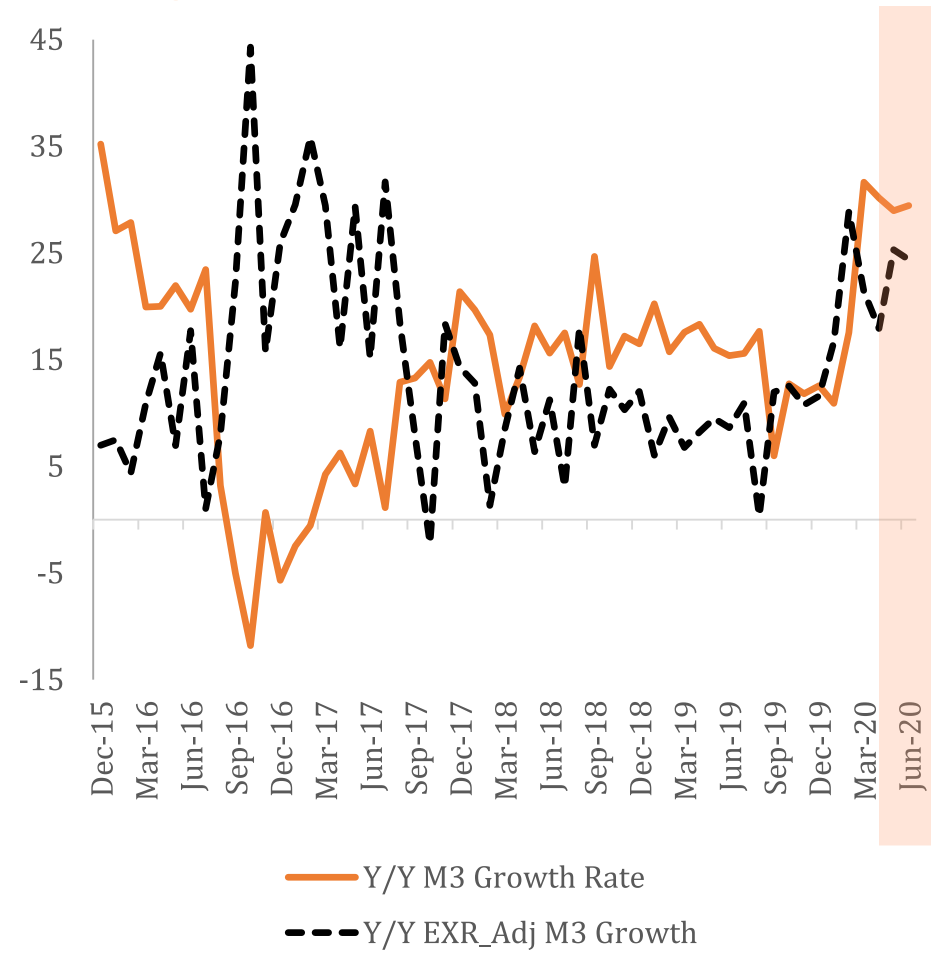



Source: Bank of Zambia

# MONEY SUPPLY

**In spite of the expansion of credit to Government, year-on-year, money supply growth slowed down to 29.4% in June 2020 from 31.6% in March.**

**Figure 13: Money Supply Growth**




Source: Bank of Zambia

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**The ongoing fiscal spending pressures were compounded by measures taken to contain the COVID-19 pandemic.**

**At the same time, the pandemic has precipitated a sharp drop in revenue.**

**In light of the high external debt and expansion in domestic borrowing, bringing the fiscal deficit to sustainable levels has become even more challenging.**

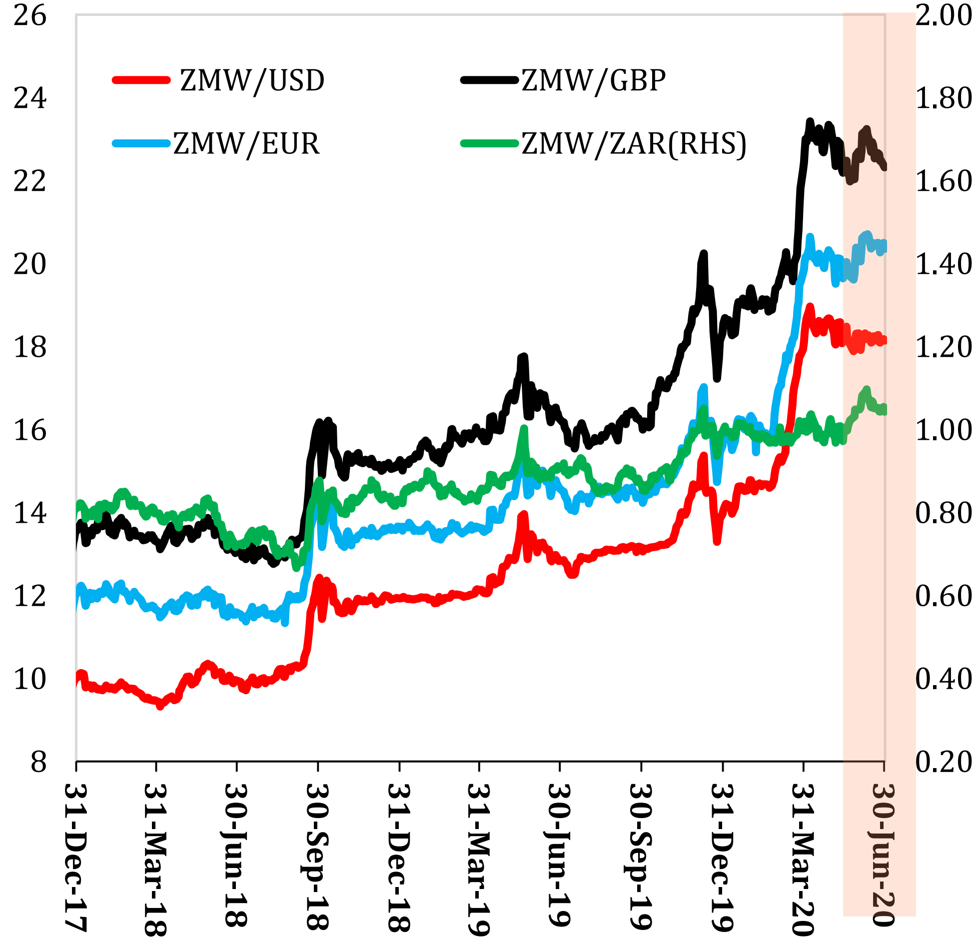
**To restore macroeconomic stability and achieve sustainable economic development, urgent macroeconomic adjustment measures, underpinned by fiscal consolidation and the restoration of debt sustainability, therefore, remain imperative.**

## FOREIGN EXCHANGE MARKET

**After coming under severe pressure in the first quarter, the exchange rate of the Kwacha to the United States dollar rose to above K18.00/US$ at the beginning of the second quarter and subsequently stabilised around K18.20/US$ over the remainder of the quarter (Figure 13).**

**The Bank has continued to provide measured market support to the Kwacha to moderate exchange rate fluctuations.**

Figure 14: Nominal Exchange Rates

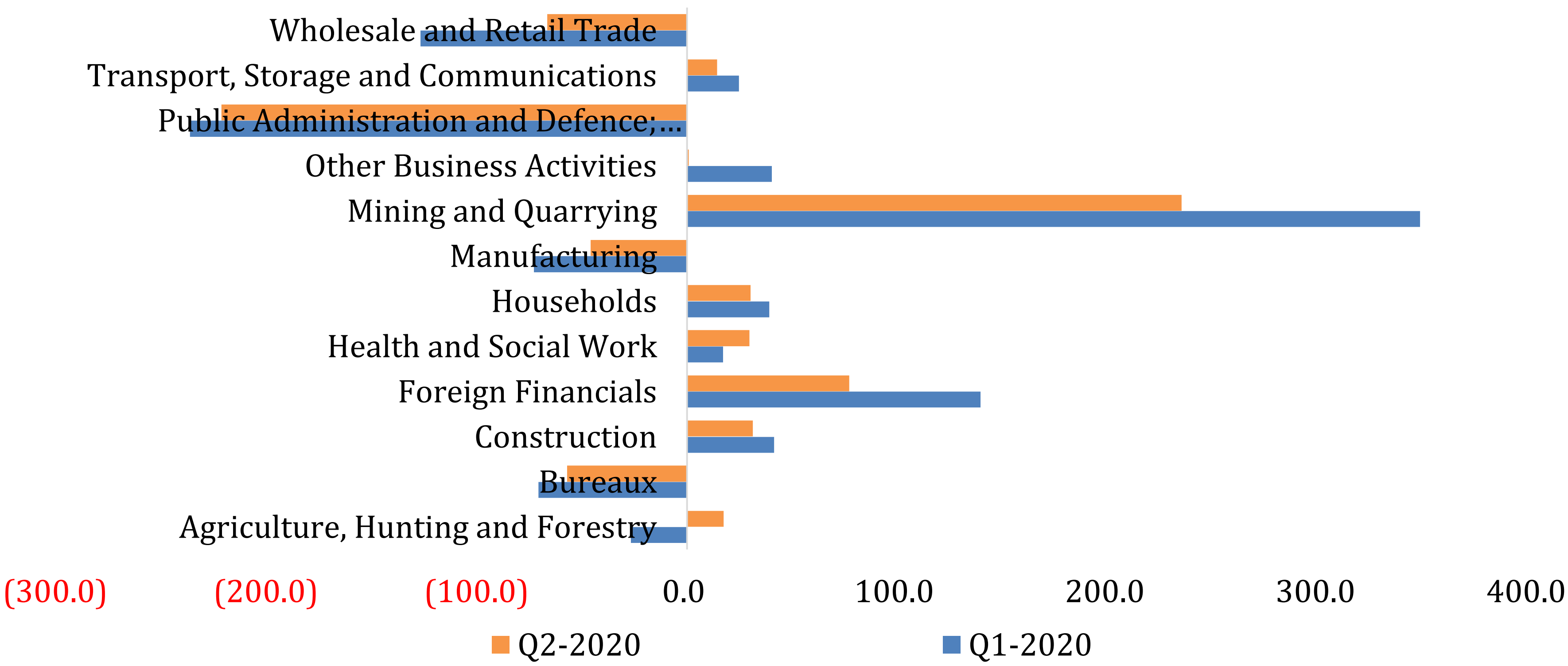



Source: Bank of Zambia

# FOREIGN EXCHANGE MARKET

**The supply of foreign exchange from the mines and foreign financials declined. Demand also fell, particularly from the wholesale and trade sector, reflecting subdued economic activity.**

**Figure 15: Foreign Exchange Net Supply by Sector (US$')**




Source: Bank of Zambia

# SELECTED COMMODITY PRICES

**Commodity prices declined as global demand weakened in response to containment measures taken across the world to slowdown the spread of COVID-19.**

**Figure 16: Commodity Prices**

| | 2019 Q1 | 2019 Q2 | 2019 Q3 | 2019 Q4 | 2020 Q1 | 2020Q2 |
|---|---|---|---|---|---|---|
| Copper Price (US$/ton) | 6,226.0 | 6,113.0 | 5,803.0 | 5,898.0 | 5,634.0 | 5,351.0 |
| Oil Price (Dubai) (US$/barrel) | 63.4 | 67.0 | 60.9 | 61.4 | 50.7 | 31.7 |
| Wheat (US$/ton) | 211.5 | 201.7 | 189.0 | 204.5 | 216.3 | 207.7 |
| Maize Price (US$/ton) | 167.5 | 175.9 | 170.1 | 166.8 | 167.6 | 146.3 |
| Cotton (US$/kg) | 1.8 | 1.8 | 1.6 | 1.7 | 1.6 | 1.5 |
| Sugar (US$/kg) | 0.28 | 0.28 | 0.27 | 0.28 | 0.30 | 0.24 |
| Soya beans (US$/ton) | 377 | 353 | 366 | 380 | 378 | 363 |

## CURRENT ACCOUNT DEVELOPMENTS

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**Current account surplus narrowed to US$210.3 million (1.3% of GDP) from US$446.2 million (2.8% of GDP), driven by deficits on the *primary income* and *services* accounts, which outweighed the improvement in the *balance of goods* surplus.**

**Figure 17: Balance of Payments (Quarterly Change - US$ million)**

| | Q1 2019 | Q2 2019 | Q3 2019 | Q4 2019 | Q1 2020 | Q2 2020 |
|---|---|---|---|---|---|---|
| Current Account Balance | **-7.2** | **2.2** | **73.5** | **78.2** | **446.2** | **210.3** |
| Balance on Goods | **288.2** | **206.0** | **-4.1** | **254.3** | **362.9** | **597.4** |
| Total Goods Exports | **1,926.6** | **1,885.1** | **1,612.3** | **1,822.0** | **1,673.6** | **1,626.0** |
| Copper | 1,431.9 | 1,320.3 | 1,013.8 | 1,228.6 | 1,188.5 | 1,200.8 |
| Cobalt | 3.3 | 0.0 | 0.0 | 39.4 | 1.0 | 7.0 |
| Gold | 43.2 | 46.0 | 50.1 | 57.1 | 49.5 | 59.5 |
| NTEs | 429.4 | 500.1 | 529.6 | 478.2 | 415.7 | 346.6 |
| Total Imports | **1,638.4** | **1,679.2** | **1,616.4** | **1,567.8** | **1,310.7** | **1,028.6** |
| Primary Income | **-225.2** | **-131.8** | **100.3** | **-143.3** | **120.0** | **-336.7** |
| Secondary Income | 77.0 | 81.4 | 82.9 | 81.1 | 47.6 | 56.1 |
| Services Account | **-147.2** | **-153.4** | **-105.7** | **-113.9** | **-84.5** | **-106.5** |
| Capital Account | 17.9 | 39.9 | 19.5 | 19.3 | 23.1 | 20.8 |
| Financial Account | 188.4 | -46.1 | -82.4 | 173.5 | 598.2 | 186.4 |
| Net Errors/Omissions | 16.3 | -17.2 | -110.7 | 2.3 | 19.0 | -17.1 |
| Overall Balance | **161.3** | **-70.9** | **-64.7** | **73.8** | **109.8** | **-27.7** |
| Change in Reserve Assets | -163.9 | 44.0 | 62.1 | -85.9 | -112.4 | 22.6 |

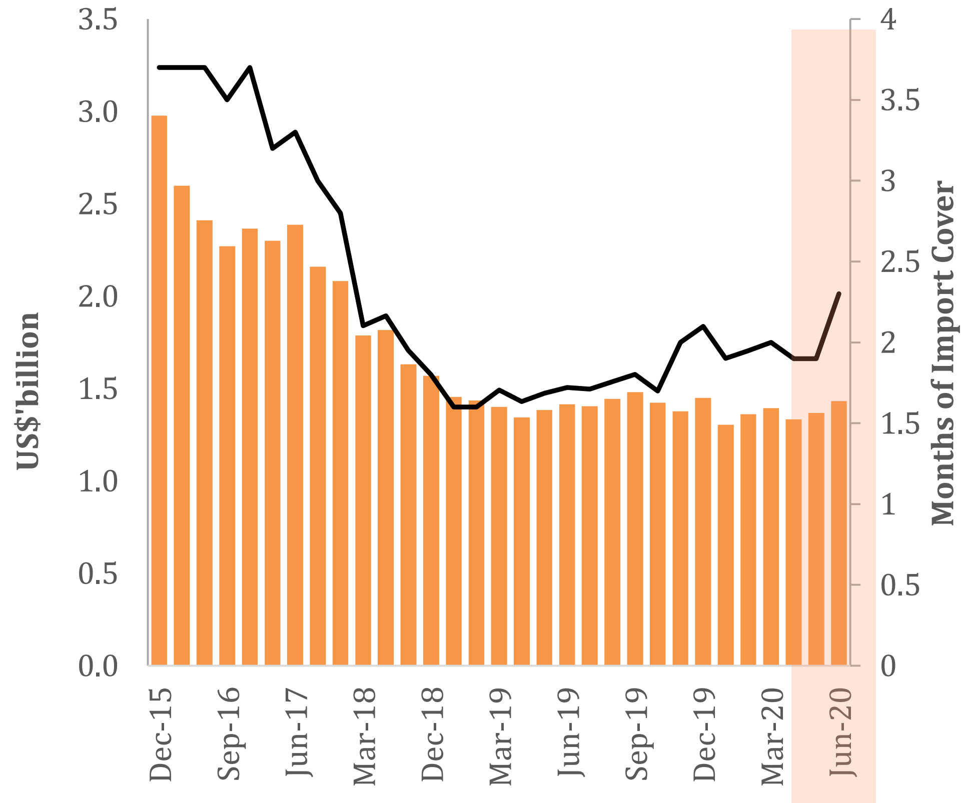
Source: Bank of Zambia

## GROSS INTERNATIONAL RESERVES

**At end-June 2020, Gross International Reserves increased to US$1.43 billion (equivalent to 2.3 months of import cover) from US$1.40 billion (equivalent to 2.0 months of import cover) at end-March 2020.**

**Mining tax receipts (including mineral royalty tax) and net foreign exchange purchases from the market mainly account for the increase in reserves.**

**Figure 18: Gross International Reserves**




Gross (Unecumbered Reserves & Encumbered Reserves at Market Rate in U.S$ billions)

Months of import cover for GIR (RHS)

Source: Bank of Zambia

# CONCLUSION

**The MPC decided to cut the Policy Rate by a further 125 basis points to 8.0%. In arriving at the decision, the Committee took into account:**

- **the need to safeguard financial stability, people's lives and livelihoods in the wake of the COVID-19 pandemic;**
- **the projected steady decline in inflation towards the upper bound of the medium-term target range at the end of the forecast period;**
- **significant worsening in economic conditions over the second quarter, and much weaker growth prospects in 2020 than earlier anticipated.**

**The Committee, thus, reiterates the need for concerted efforts among all stakeholders to effectively deal with the COVID-19 pandemic. In this context, urgent macroeconomic adjustment measures underpinned by fiscal consolidation and the restoration of debt sustainability remain imperative to promote sustainable development and save peoples' lives**

# THANK YOU

# GOD BLESS…

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