REMARKS BY THE GOVERNOR

ON THE LAUNCH OF THE 2023 BANKING INDUSTRY SURVEY REPORT BY PwC

August 2024

Bank of Zambia

PRESENTATION OUTLINE

- Introduction
- State of the Local Economy
- Liquidity risk
- Cybersecurity
- Financial performance and condition of the sector

INTRODUCTION

- The Survey is a very useful tool to many stakeholders, including ourselves.

- The 2023 Report is the **Eighth edition.** We commend Pwc for this initiative and we appreciate the cooperation of the respondents.

- The 2023 Survey Report raises a lot of important issues. However, will focus our brief comments on **three top issues** raised by respondents:

  - State of the local economy;
  - Liquidity risk; and
  - Cybersecurity

STATE OF THE LOCAL ECONOMY

- Will look at the state of the local economy through the lens of our recent Monetary Policy Committee meeting.

- The MPC maintained the Monetary Policy Rate at 13.5 percent. While actual and projected inflation remain elevated relative to the 6-8 percent target band, the Committee judged that the current monetary policy stance is appropriate.

- **Inflationary pressures** have persisted, with inflation rising to an average of 14.6 percent in the second quarter of 2024 from 13.5 percent in the first quarter.

- Persistent depreciation of the Kwacha against major currencies and rising prices of food (maize grain, maize products, and vegetables) and energy, particularly fuel, due to constrained supply continued to drive inflation up.

- These factors remain key risks to the inflation outlook, exacerbated by extended hours of electricity load management, continued geopolitical conflicts and tight global financial conditions.

- Inflation is, however, forecast to moderate to 12.7 percent in 2025, albeit higher than the 9.8 percent reported in the May 2024 Monetary Policy Report.

- In the first half of 2026, inflation is expected to average 10.8 percent.

STATE OF THE LOCAL ECONOMY (Cont.)

- **The MPC decision further considered the impact of the drought** and that of the past successive increases in PR, increases in SRR, and the recent reforms in fx market.

- In maintaining the PR as opposed to raising it, the Committee also considered the impact on financial stability and growth, particularly in 2024, in the wake of the drought.

- Continued implementation of fiscal consolidation measures and structural reforms remains critical to lowering inflation, maintaining financial stability, and creating growth enabling environment and resilience of the economy against shocks.

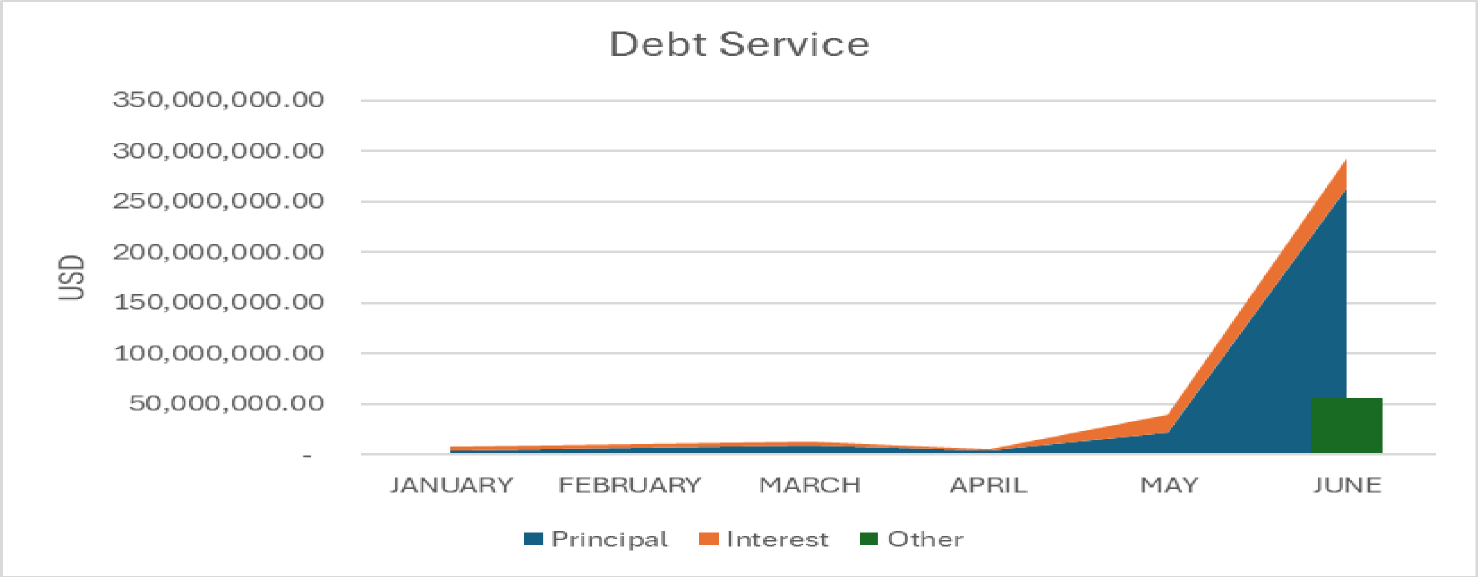
- To safeguard macroeconomic stability needs concerted efforts and strengthened collaboration among all stakeholders.

- Prospects in the medium to long-term are very positive. Need to continue with the reform process can hardly be overemphasised.

Status of debt service

- In quarter 1 of 2024 debt service was only to multilateral and plurilateral institutions .

- In the second quarter, there was a sharp upward jump following the conclusion of restructuring of the Commercial (Eurobond Holders) as broader debt service resumed (see chart below).



LIQUIDITY RISK

Secondly, the industry's concerns on liquidity risk is noted. However, it is important to fully appreciate the context that informed BoZ actions.

- The environment has for sometime now been characterized by strong underlying inflationary pressures, stemming not only from the debilitating drought shock of 2023/24 agricultural season, but also the persistent exchange depreciation.

- Managing such pressures points to the need to implement relatively tight monetary policy to contain the inflationary pressures.

- We are the first to admit that the Policy Rate, **on its own,** is not sufficient to manage exchange rate pressures. The Bank has had to complement the policy rate changes with upward adjustments in the Statutory Reserve Ratio. In this regard, in early February 2024 we raised the SRR to 26% from 17% on 5 February 2024.

- At the same same time it was deemed necessary that the Government transfers its unutilised deposits from commercial banks to the BoZ. Thus, on 29 January 2024, commercial banks were instructed to transfer such deposits to BoZ.

- The increased Statutory Reserve Ratio resulted in a net withdrawal of K8.1 billion of excess liquidity. With respect to Government deposit transfers, between end-January 2024 and July 2024 K3.4 billion had been transferred to BoZ —far much less than the projected K12 billion.

LIQUIDITY RISK (Cont.)

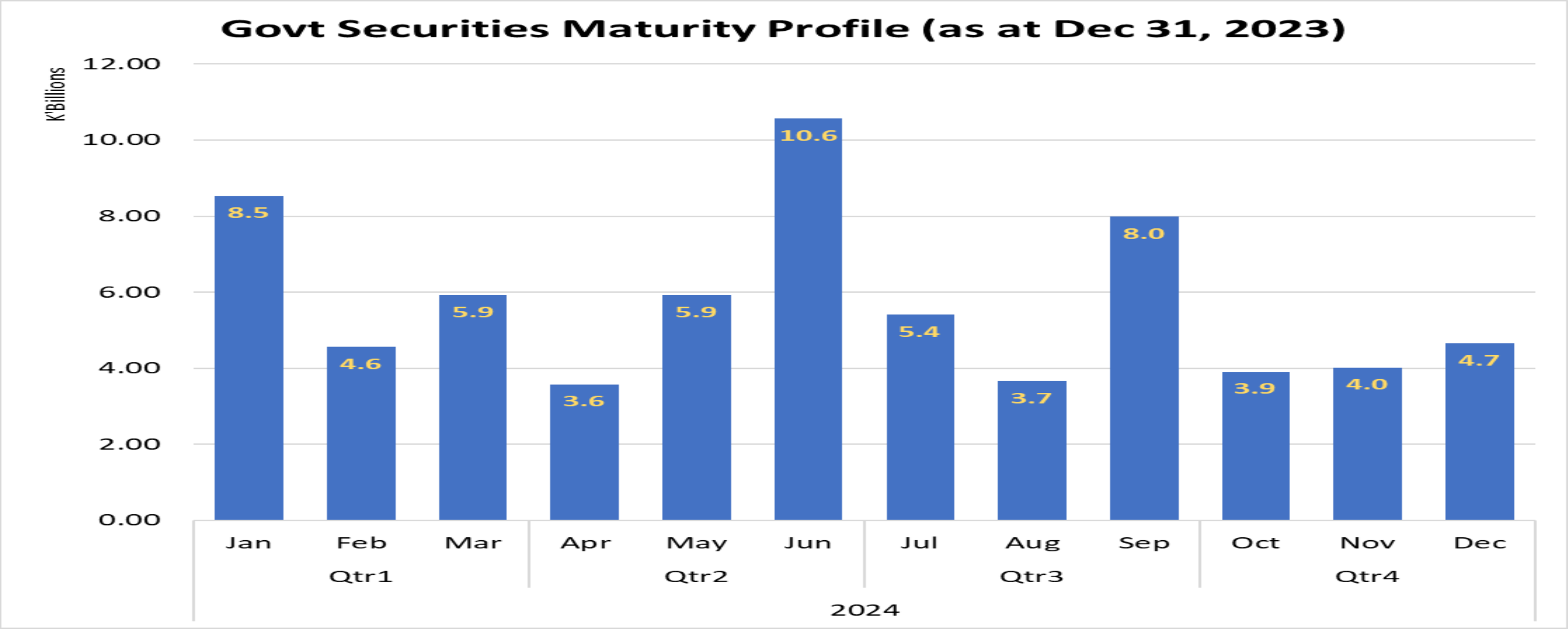
- **The less-than-satisfactory performance of the Government deposit transfers meant that the impact was not fully achieved. With** this development another way of achieving the intended objective had to be found. The Bank turned to making Overnight Lending Facility (OLF) as the main source of commercial banks' liquidity as opposed to use of regular Open Market Operations (OMO).

- Upon observing relative stability in the foreign exchange market conditions since June 2024, the Bank started to provide commercial banks liquidity relief through the much cheaper OMO facility compared with the OLF (OMO loans currently cost 13.5% whereas OLF is at 30%).

- Further relief came by way of restructuring how statutory reserve ratio compliance is to be achieved. This measure was taken within the context of safeguarding financial stability.

LIQUIDITY RISK (Cont.)

- In June this year, the Bank invited commercial banks to participate in a limited auction of Government bonds up to 40.0 percent of their respective minimum kwacha statutory reserve requirement.
- The Government bonds purchased in this particular auction are eligible for statutory reserve requirement purposes. This measure has, so far, moderated the cost of complying with the statutory reserve requirements. But more importantly, risks to financial stability have been contained by safeguarding an orderly functioning of the Government securities market, especially in the face of large maturities that came due mid-year
- Overall, the Bank maintained tight liquidity conditions for the most part of the year-to-date to support the foreign exchange market and tame inflation.



CYBERSECURITY

Cybersecurity has remained a concern for the sector, at least for the past three banking surveys, as product offerings from the sector continue to evolve at a rapid pace towards digital solutions.

- At the back of the increased reliance on digital channels for product offerings and services, is the heightened risk of cyberattacks.

- Banks are taking deliberate measures to strengthen their cyber defence mechanisms by investing in relevant infrastructure as well as enhancing customer and staff awareness programmes.

- The Bank of Zambia launched its 2024-2027 Strategic Plan with a theme *'Promoting Inclusive and Sustainable Development in a Digitalised World'.*

- The strategy, seeks to respond to new challenges and emerging risks, and focuses on four main areas namely: Price Stability, Financial Stability, Financial Inclusion and Organisational Resilience and Growth.

CYBERSECURITY

Bank of Zambia

- One of the initiatives in our strategic plan is *Strengthening Cyber Resilience and Fraud Mitigation in the Financial Sector* by establishing the Financial Sector Cyber Incident Response Team (FINCIRT);

- This is being done in partnership with the Bankers Association of Zambia.

- The initiative will benefit the financial sector as it will provide a platform for information sharing which will promote safety and resilience of the sector

- As part of the Bank's efforts to enhance cyber resilience in our institutions and address cyber risk in the financial sector, in 2023 the Bank issued Cyber and Information Risk Management Guidelines for Regulated Entities.

- Further, the Bank has commenced Cyber security examinations across the industry, following the issuance of Guidelines in 2023.

FINANCIAL PERFORMANCE AND CONDITION OF THE SECTOR

Bank of Zambia

Despite these challenges, the banking sector remained Resilient.	Was adequately capitalised with capital adequacy ratios remaining well above the minimum requirements.
	The sector continued to generate sufficient income to cover operating costs, fund growth and augment capital.
	Liquidity conditions varied across banks and the Bank of Zambia instituted relevant support measures to the sector as alluded to earlier.
	Asset quality was **satisfactory,** however, continued to be a source of concern, and the Bank will continue to assess the situation and will institute appropriate measures to minimise disruption to the financial system.

THANK YOU

Bank *of* Zambia