Group Corporate Strategy
ZB Financial Holdings Limited
1st Floor, 21 Natal
21 Natal Road, Belgravia, Box 3198, Harare
Tel: +263 (0)8677002001

Banking | Investments | Insurance

STAYING THE COURSE TO PRICE STABILITY

(Highlights, Analysis and Implications)

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© **Group Corporate Strategy**
ZB Financial Holdings Limited
1st Floor, 21 Natal
21 Natal Road, Belgravia, Box 3198, Harare
Tel: +2638677002001

Website: www.zb.co.zw

1. INTRODUCTION

1.1. The Reserve Bank of Zimbabwe (RBZ), on 9 August 2023, issued a Mid Term Monetary Policy Review Statement primarily aimed at ensuring that the country stays on course or continues to hold on to the right path of the progress that it has attained on the "price and financial stability" fronts.

1.2. Prior to the issuance of the Mid Term Monetary Policy Statement, the country experienced significant exchange rate depreciation between April and June 2023 driven by both demand and supply factors, which exerted significant pass-through effects to inflation; and a decline in the demand for local currency due to speculative behaviour.

1.3. The unstable environment led to the introduction of bold policy intervention measures by the Government and RBZ for tackling the transitory price and exchange rate volatility.

1.4. These bold measures have gone a long way in arresting the instabilities and bringing the much-needed normalcy in the price and exchange rate dynamics and calmness in domestic markets. The measures instituted by the RBZ, which include further liberalisation of the exchange rate, tighter monetary policy and the introduction of gold coins and gold-backed digital tokens are bearing fruit as evidenced by the current firming and relatively stable exchange rate dynamics.

- ***However, we contend that the "stability" which has been attained starting from the end of Q2 2023 to-date, is premised on a rather unsustainable liquidity mopping initiative which will most likely be relaxed post-elections.***

1.5. With the aforementioned background, the RBZ issued its Mid Term Monetary Policy Review whose highlights are as follows:

- **Broadly, the RBZ has maintained its policy stance – Tight/ Contractionary monetary policy. No changes to the status quo.**

MEASURES	COMMENTARY
1. Interest Rates - The RBZ has maintained the current policy rates which will continue to be reviewed in line with inflation developments. **1.1.** The Bank RBZ policy rate is currently at 150%;	• Considering the levels of inflation (at 101.3% y-o-y), its justified to have such high interest rates in order to have real returns on lending. However, the interest rates are deterrent to genuine borrowers who would want to borrow for the long term, especially the productive sectors.

MEASURES	COMMENTARY
1.2. The medium-term accommodation lending rate for productive sectors including individuals and MSMEs is currently at 75%; **1.3.** The RBZ policy rate remains the minimum lending rate for all banks; and **1.4.** The deposit interest rates on savings and time deposits are currently at 30% and 50% per annum, respectively.	• These high interest rates have helped in curtailing ZWL$ borrowings and hence constraining money supply growth. • It is our hope that the RBZ will review the rates as per the policy statement. • **It becomes imperative for the Banking Cluster to enhance revenue generation from non-funded streams [e.g. commissions and fees], in order to counter the expected continued reduction in interest income. Furthermore, tightening monetary policy has adverse effects on liquidity, and ZB should not be caught unawares, but rather, be proactive and have strategic responses in place. Most importantly, ZB should intensify deposit mobilisation initiatives as well as progressing the POS Strategy to ensure POS devices are not only being deployed with high volume high value merchants, but are also being utilised optimally.** • If that monetary contraction stance is pursued in the long run, there are higher chances that macroeconomic stability could be sustained. However, judging from the previous policy shifts by the authorities, the sustainability of the measures remains in doubt.
2. Non-negotiable Certificate of Deposits - The RBZ shall strengthen the operation of the Non-negotiable Certificate of Deposits (NNCDs) which are being used to mop excess local currency liquidity through the introduction of NNCDs with maturity profiles of 7,14, 21 and 30 days.	• NNCDs are a form of open market operations by the central bank meant to mop up excess liquidity in the market. Despite the introduction of the shorter maturity profiles, the overall effect of NNCDs on the banking sector remains one of curtailing liquidity and capacity to extend credit – ZB should

MEASURES	COMMENTARY
	continue to find ways of minimising the effects of the biting liquidity situation.
3. Auction System - The foreign currency auction system remains a critical source of foreign currency for the economy. As such, the RBZ shall continue with the current auction system in place and further liberalise the use of forex from the wholesale auction system by allowing banks to meet bonafide small foreign payment requirements for their customers, including individuals and Micro, Small and Medium Enterprises (MSMEs) in order to enhance financial inclusion.	• The Auction has indeed played a critical role in the allocation of Forex, despite its flaws. More is required on the part of liberalising the auction so as to enhance the exchange rate discovery mechanism and also to accommodate individuals and companies trading outside the official system. • An accommodative Auction system will go a long way in closing the gap between alternative and official rates and also in bringing to the official channels the US Dollars exchanging hands outside official systems.
4. Statutory Reserve Requirements: The Statutory reserve requirements have been maintained at the current rates as follows**.** **4.1.** Foreign currency demand and call deposits, 10%; **4.2.** Foreign currency time and savings deposits, 5%; **4.3.** Domestic currency demand and call deposits, 15%; and **4.4.** Domestic currency time deposits, 5%.	• Statutory Reserves may in simpler terms be defined as a fraction of deposits that Banks need to keep with the RBZ and cannot be onward lent. On that note, a high statutory reserve ratio means less is available for on-lending. More so, considering the transitory nature of deposits, maintaining high statutory Reserve requirement ratios further exacerbates liquidity issues for Banks. This measure (and the other tight monetary policy initiatives) has largely left the banking sector, and ZB in particular, grappling for liquidity especially in terms of local currency.
5. Other Monetary Policy Measures **5.1.** Localising Tobacco Production Financing - There will be no restrictions on the use of locally sourced funds to support	• Localisation of Tobacco production financing provides an opportunity for local players that include Banks to structure mutually beneficial relationships with tobacco farmers.

MEASURES	COMMENTARY
the production of tobacco in the country with immediate effect. **5.2.** Regularisation of Tourism Agreements with External Partners **-** The RBZ is granting a moratorium to all tourism operators who have unregistered tourism agreements and unapproved offshore accounts to regularise the agreements and offshore foreign currency accounts before 31 August 2023. **5.3.** Gold coins and gold-backed digital tokens **-** The Bank will undertake an awareness campaign in all the national provinces in preparation for Phase II (Transactional Phase) of the Gold-Backed Digital Tokens (GBDT), which is at an advanced stage. The transactional phase will complement the use of both ZW$ and US dollar in the domestic economy and run under the code or name ZiG, for Zimbabwe Gold.	• The moratorium to all tourism operators is a reprieve to the sector and players should utilise the opportunity to regularise their operations. • Banks should be prepared in terms of the necessary systems and structures for the transactional phase of the Gold Backed Digital Tokens (GBDT) or ZiG. The 'early birds' and those prepared with regards to infrastructure stand to benefit more in these kinds of transactions. ZB should therefore strive to be counted amongst the "early adopters" rather than be a laggard, and the Group's Digital Transformation drive puts ZB in a good position to adopt GBDT. • In essence, the authorities appear to be setting the tone and preparing minds for possible introduction of a "digital currency" backed by gold.

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