Bank of Zambia

MONETARY POLICY COMMITTEE STATEMENT

[*This Statement is issued pursuant to Section 29(1) of the Bank of Zambia Act, 2022*]

Monetary Policy Rate raised to 10.0 percent from 9.5 percent

The Monetary Policy Committee, at its August 21-22, 2023 Meeting, ***decided to raise the Monetary Policy Rate by 50 basis points to 10.0 percent****. The decision was informed by the movement of current and projected inflation away from the 6-8 percent target band and the need to contain inflation expectations.*

Inflation increases in the second quarter of 2023 as inflationary pressures persist

After declining for six consecutive quarters, inflation rose to an average of 9.9 percent in the second quarter of 2023 from 9.6 percent in the first quarter, moving away from the 6-8 percent target band. The lagged pass-through from the depreciation of the Kwacha against the US dollar, higher maize grain and meat prices, reduced supply of vegetables, and the upward adjustment in electricity tariffs explain this outturn.

In July, inflation accelerated to 10.3 percent from 9.8 percent in June, moving further away from the target band as some of the upside risks identified in the May MPC Meeting materialised during the second quarter.

Inflationary pressures are expected to persist over the forecast horizon[1], with inflation projected to average 10.2 percent in 2023 and 9.3 percent in both 2024 and the first half of 2025, well above the 6-8 percent target band. This path of inflation is broadly higher than that of the May 2023 forecast. Elevated maize grain prices and tight global financial conditions are the key drivers of the current inflation outlook. The foregoing factors as well as higher global food and energy prices due to the prolonged Russia-Ukraine war remain key upside risks.

Whilst the Kwacha appreciated by 4.8 percent against the US dollar in the second quarter, it depreciated by 11.0 percent to K19.48 between end-June and August 22, 2023. The positive market sentiments related to the external debt restructuring agreement reached with the Official Creditors to Zambia under the G20 Common Framework for debt restructuring notwithstanding, the market has continued to be characterised by low supply of foreign exchange amid rising demand as the economy recovers post-COVID-19 pandemic. To moderate exchange rate volatility and support critical imports, the Bank continued to provide liquidity to the market. In the second quarter, US$300 million was provided to the market, largely from mining sector tax receipts (US$242 million). This, coupled with Government uses of foreign exchange and external debt servicing, led

[1] The forecast horizon is from the third quarter of 2023 to the second quarter of 2025.

August 23, 2023

Bank Square, Cairo Road, P.O. Box 30080, Lusaka, Zambia Tel:+260-211-399300, E-mail: info@boz.zm. Web: http://www.boz.zm

to the decline in gross international reserves to US$2.7 billion (equivalent to 2.9 months of import cover) at end-June 2023 from US$2.9 billion (equivalent to 3.3 months of import cover) at end-March 2023.

Interest rates rise, growth in credit and money supply slows

During the second quarter, interest rates rose, broadly in line with the upward adjustment in the Monetary Policy Rate in May 2023. The overnight interbank rate marginally increased to 9.39 percent at end-June from 9.26 percent at end-March. Over the same period, commercial banks' average lending rate edged upwards to 25.7 percent from 25.5 percent. Growth in domestic credit and money supply slowed down to 9.1 percent and 17.5 percent, year-on-year, in June from 12.1 percent and 30.0 percent in March, respectively. This largely reflected the lower Kwacha value of foreign currency deposits following the appreciation of the exchange rate of the Kwacha against the US dollar (valuation effects).

Economic activity moderates, but projected to rebound in the medium-term

Preliminary information from the *August 2023 Bank of Zambia Quarterly Survey of Business Opinions and Expectations (QSBOE)* and the *Stanbic Bank Zambia PMI™* point to improved economic activity in the second quarter of 2023. Nonetheless, the *QSBOE and PMI* suggest a potential slowdown in economic activity in the third quarter of 2023 due to reduced output in some sectors.

In 2023, GDP growth is projected to be lower due to a further contraction in the mining sector as well as the slowdown in the education and electricity sectors. However, growth is expected to pick-up over the medium-term (2024-2025), underpinned by the projected recovery in the mining sector and sustained growth in the information and communications, financial and insurance as well as wholesale and retail trade sectors.

Current account deficit widens, but projected to rebound in the medium-term

The *current account* deficit widened to US$198.1 million in the second quarter from US$188.7 million in the first quarter, largely driven by the rise in imports as exports declined and credit on income attributable to financial corporations, non-financial corporations, and households also reduced. For 2023, the *current account* is projected to record a deficit of US$0.9 billion, mostly due to a sharp decline in export earnings, while imports continue to recover post-COVID-19 pandemic. However, in the medium-term, the current account is projected to recover as net exports rebound.

Bank Square, Cairo Road, P.O. Box 30080, Lusaka, Zambia Tel:+260-211-399300, E-mail: info@boz.zm. Web: http://www.boz.zm

Bank *of* Zambia

Monetary Policy Committee Decision

To reiterate, the Monetary Policy Committee, at its August 21-22, 2023 Meeting**, decided to raise the Monetary Policy Rate by 50 basis points to 10.0 percent.** This is in recognition that inflation not only persisted above the 6 - 8 percent target band during the second quarter, but moved further away from the target in July 2023. It is currently projected to remain above the target band over the forecast horizon. Left unchecked, this would undermine the gains already made in restoring macroeconomic stability.

The Committee recognises the significant structural reforms undertaken by the Government, which are reflected in lower fiscal deficits, debt restructuring, and broader efforts to promote investment and private sector led growth. Monetary policy can best support these efforts by steering inflation back to the target band and anchoring inflation expectations. This is consistent with the Bank of Zambia mandate to achieve and maintain price and financial system stability.

The Committee noted that the financial sector exposure to systemic risk is moderate and it will remain relatively well capitalised. Further, the Bank is undertaking financial sector reforms that will support financial intermediation and inclusion. These measures will support the entrenchment of macroeconomic stability and the structural reforms being undertaken by the Government.

Decisions on the Policy Rate will continue to be guided by inflation outcomes, forecasts, and identified risks, including those associated with financial stability and external debt restructuring.

The next MPC Meeting will take place on November 20 and 21, 2023.

Issued by

Dr. Denny H. Kalyalya
GOVERNOR

August 23, 2023

Bank Square, Cairo Road, P.O. Box 30080, Lusaka, Zambia Tel:+260-211-399300, E-mail: info@boz.zm. Web: http://www.boz.zm